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In The

Supreme Court of the United States

October Term, 1990

COMMISSIONER OF REVENUE SERVICES
OF THE STATE OF CONNECTICUT,

Petitioner,

v.

SFA FOLIO COLLECTIONS, INC.,

Respondent

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF CONNECTICUT

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QUESTION PRESENTED

Whether the systematic and continuous solicitation and exploitation of the Connecticut consumer market by the Respondent out-of-state mail order company constitutes sufficient nexus for purposes of the Due Process and Commerce Clauses to require the Respondent to collect use taxes from Connecticut customers on goods sold for use within the state.

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SFA FOLIO COLLECTIONS, INC.,

Respondent

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF CONNECTICUT

The petitioner, Commissioner of Revenue Services of the State of Connecticut, respectfully prays that a writ of certiorari issue to review the judgment and opinion of the Supreme Court of the State of Connecticut entered on January 22, 1991.

OPINIONS BELOW

The opinion of the Supreme Court of the State of Connecticut is reported at 217 Conn. 220, ____ A.2d ____ (1991), and is reprinted in the appendix hereto, p. A1.

The Memorandum of Decision of the Superior Court of the State of Connecticut was issued on April 20, 1990, and has not been reported. It is reprinted in the appendix hereto, p. A21.

JURISDICTION

The decision of the Supreme Court of Connecticut, affirming the judgment of the Superior Court of Connecticut, was entered January 22, 1991. This petition is filed within 90 days of this judgment, as allowed by 28 U.S.C. § 2101(C) and U.S. Supreme Court Rule 13.1.

The jurisdiction of this Court to review the judgment of the Supreme Court of the State of Connecticut is invoked under 28 U.S.C. § 1257.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

This case involves the following constitutional and statutory provisions: U.S. Const. Art. I, § 8; U.S. Const. Amend. XIV, § 1; and Conn. Gen. Stat. § 12-422.

The text of said provisions is reproduced in the appendix in accordance with U.S. Supreme Court Rule 14.1(f).

STATEMENT OF THE CASE

Petitioner, the Commissioner of Revenue Services of Connecticut, has sought to impose use tax on an out-of-state mail order seller, SFA Folio Inc., for mail order sales to Connecticut residents.

The parties (hereinafter "the Commissioner" and "Folio") stipulated to all of the facts relating to these proceedings. There was no testimony except the deposition of Joan F. Krey, an officer of Folio and vice president, general counsel, and secretary of Saks & Company, Folio's parent corporation, which was submitted as an exhibit by both parties.

Based upon this deposition and the Stipulation of Facts, App. p. A29, and exhibits thereto, the factual background can be summarized as follows.

Because of the large-scale, systematic, continuous solicitation and exploitation of the Connecticut consumer market by Folio, the Connecticut Commissioner of Revenue Services required Folio to collect use taxes from its Connecticut customers. There is no dispute between the parties that purchases and subsequent use of the property is subject to tax. The only question is whether Folio must collect it.

Folio is a corporation organized and existing under the laws of the State of New York with its principal place of business in Yonkers, New York. It is a wholly-owned subsidiary of Saks & Company ("Saks"), which is a New York corporation with its corporate headquarters in New York City. Folio is an affiliate of Saks Fifth Avenue – Stamford, Inc. ("Saks-Stamford"), a Connecticut corporation which is also wholly-owned by Saks and which operates a Saks store in Stamford, Connecticut.

Folio engages in mail order catalog sales from its place of business in Yonkers. Written or telephone purchase orders from Connecticut residents are received in Yonkers. Folio operates a toll-free "800" telephone number for its customers to use to place their orders. Folio sends mail order catalogs and flyers to Connecticut residents. In the pertinent

years 1986 and 1987, approximately 649,000 and 733,000 catalogs, respectively, were sent to Connecticut residents. Folio has also contracted with companies which place ads to sell Folio catalogs several times a year in national fashion magazines. These companies sell the mail order catalogs they advertise in these magazines. Extra copies of Folio mail order catalogs are shipped to the Saks Fifth Avenue store in Connecticut for general managers to use as reference guides, to inform employees of fashion trends, and to provide merchandise information. Tailoring services are available at the Stamford store to Folio customers. The Saks Fifth Avenue store in Stamford also sells merchandise identical to that sold by Folio.

Customers pay for their Folio orders by check or money order or by using their American Express, Visa, MasterCard, Diners Club, or Saks Fifth Avenue credit cards. A Folio customer may obtain a Saks Fifth Avenue charge account application through the Folio mail order form. The credit department of Saks includes advertising pieces, called "bill inserts," in the same envelope as charge account statements sent to customers. These bill inserts contain the toll-free number of Folio. To the extent any sales are generated from Connecticut customers who receive bill inserts, the sales are filled by Folio. Folio pays the cost of the customer return envelope for the billing statement.

"SFA" is an abbreviation for Saks Fifth Avenue. It is part of Folio's name (*SFA* Folio Collections, Inc.) and is used with the permission of its parent corporation, Saks. The name "Saks Fifth Avenue" appears in the Folio mail order catalogs. The distinctive script designs of "Saks Fifth Avenue" and "SFA" are owned by the parent company, Saks.

Folio and Saks share common directors and officers. The same is true of Folio and Saks Fifth Avenue-Stamford, Inc. The Saks Fifth Avenue store in Stamford and Folio share a great variety of daily sales data, monthly sales summaries, and sales inventory levels by category and type of merchandise. They also share financial data and profit and loss statements.

Folio utilizes Saks charge card listings for use in deriving its mailing list. Saks maintains a distribution center in Yonkers, New York, which receives inventory to be distributed to 45 Saks retail stores, including the one in Stamford, Connecticut, and to Folio. The Folio catalog is designed with the help of corporate advertising and corporate marketing, a department of Saks which also aids the Saks Stamford store with its mailings and store catalogs. Decisions as to buying and marketing of merchandise are made with the advice and counseling of Saks executives. Finally, Folio benefits from the use of the Saks Fifth Avenue and SFA trademarks.

As a business entity in and of itself, Folio was assessed the sales and use tax because of the significant commercial contacts it had maintained with the State of Connecticut, and for the services provided by the State, as well as the economic presence demonstrated by the one and a third million catalogs sent into a state of less than three and a half million people of all ages and of all social and economic conditions. In addition, the assessment is also justified as not being in contravention of the Constitution because the group of Saks' corporations, including Saks & Co., the parent/holding company, Folio and Saks-Stamford, are operated as a single retail enterprise, albeit utilizing separate corporations. As a single commercial enterprise, there

is tax nexus with Connecticut given the large department store located within the state.

The Respondent appealed the assessment to the Superior Court of Connecticut under the authority of Conn. Gen. Stat. § 12-422 which provides for a *de novo* trial. *Kimberly-Clark Corp. v. Dubno,* 204 Conn. 137, 144, 527 A.2d 679, 682 (1987). The trial court held for the Respondent based upon this Court's ruling in *National Bellas Hess v. Department of Revenue,* 386 U.S. 753 (1967), and the Connecticut Supreme Court case of *Cally Curtis Co. v. John G. Groppo, Commissioner of Revenue Services,* 214 Conn. 292, 572 A.2d 302 (1990), *cert. denied,* _____ U.S. _____, 111 S.Ct. 77 (1990). The Connecticut Supreme Court affirmed this judgment, 217 Conn. 220, 585 A.2d 666 (1991).

REASONS FOR GRANTING THE WRIT

THE ECONOMIC AND TECHNOLOGICAL DEVELOPMENTS IN THE MAIL ORDER BUSINESS SINCE THE DECIDING OF *NATIONAL BELLAS HESS V. DEPARTMENT OF REVENUE* IN 1967 WARRANT A RECONSIDERATION OF ITS HOLDING IN AN AREA OF TAX LAW WHICH IS OF VITAL IMPORTANCE, NOT ONLY TO CONNECTICUT BUT TO ALL STATES WITH A SALES AND USE TAX.

Nearly a quarter of a century ago, this Court decided that a mail order seller which does not maintain an actual physical presence in a state may not constitutionally be required to collect that state's sales and use tax on sales within the state. *National Bellas Hess, Inc. v. Dept. of Revenue,* 386 U.S. 753 (1967). In the twenty-four years since that decision,

mail order sales have exploded into a major industry impacting significantly on the economic climate of the nation and creating an economic presence within individual states which is often substantially more significant than mere physical presence. Also in the intervening years, technological advances in computer software have rendered once complex and time-consuming calculations a quick and easy exercise.

Due to these developments, state courts around the country are being forced to confront this issue head-on with inconsistent conclusions. In fact, a trial court in Tennessee has distinguished *Bellas Hess* based on these developments in a case involving the very company at issue here, SFA Folio Collections. *SFA Folio Collections, Inc. v. Huddleston,* No. 89-3015-III (Ch. Tenn. March 11, 1991) (*see* further discussion, *infra* at page 12).

Because of the reality of the present day mail order business not existing in 1967 and its impact on state tax collections, the Petitioner asks this Court to revisit its decision in *Bellas Hess* and fashion a nexus test for state tax purposes which reflects the evolution of both the industry itself and concepts of due process.

At the least, the Petitioner asks the Court to hold that, in the circumstances of this case, where the Respondent mail order company not only actively and frequently solicited sales within Connecticut by means of its catalogs but also was part of a corporate enterprise containing an affiliate store located within the state, sufficient nexus exists to justify the collection of the use tax on all mail order sales.

In *Bellas Hess* the Court held that the Illinois use tax at issue failed to satisfy the Constitution in two related ways.

First, the Court found that it violated the Constitution because the mail order company had insufficient connection with, and received too little benefit from, the state to warrant the imposition of a tax collection responsibility on mail order sales. Second, the Court held that the use tax collection duty violated the Commerce Clause by placing a burden on interstate commerce unrelated to any benefits that the company received from the state. In reaching its conclusion, the Court focused primarily on two things: the lack of any physical property of the mail order company within the taxing state, and the burden on interstate commerce caused by what the Court viewed as a "virtual welter of complicated obligations" in administering the tax collections. *Id.* at 759-60. In both of these areas, the passage of time has wrought significant changes.

The focus of the first – the lack of property located within the taxing state – reflected the then-current emphasis on physical presence as the touchstone in due process analysis, whether in the taxing or jurisdictional arenas. In the intervening years, however, jurisdictional jurisprudence has come to focus on (1) whether the commercial actor's activities are "purposefully directed toward" residents of the state, *Asahi Metal Industry Co., Ltd. v. Superior Court of California,* 480 U.S. 102, 112 (1987); *Burger King Corp. v. Rudzewicz,* 471 U.S. 462, 473-75 (1985); and *Keeton v. Hustler Magazine, Inc.,* 465 U.S. 770, 774 (1984); and (2) whether activities that are performed by or on behalf of the taxpayer "are significantly associated with the taxpayer's ability to establish and maintain [an in-state] market . . . for the sales."

Tyler Pipe Industries, Inc. v. Washington Department of Revenue, 107 S.Ct. 2810, 2822 (1987).[1]

Simple physical presence within a state often is unrelated to the size and significance of a corporation's economic presence in and benefit from a state. Under the holding of *Scripto, Inc. v. Carson,* 362 U.S. 207 (1960), it seems clear that if the Respondent had a few in-state agents soliciting sales, that connection alone would be sufficient nexus to justify a use tax collection duty. Yet the reality here is that the Respondent's economic presence in Connecticut is many times more substantial than the *Scripto* presence. In the space of two years, Folio distributed over 1.3 million catalogs in a state whose population is less than 3.5 million. By means of a toll-free "800" telephone number, Folio has made catalog shopping a convenient in-home activity and, by means of an in-state affiliate sharing the same distinctive corporate logo, much of the same merchandise, and the same Saks Fifth Avenue charge account service, Folio has taken significant measures to entice the Connecticut consumer to purchase its products.

The very size and aggressiveness of this solicitation reflects the development in the mail order business since *Bellas Hess* was decided twenty-four years ago. At that time, national mail order sales amounted to $2.4 billion. 386 U.S. at 763 (Fortas, J., dissenting). Such sales for 1983 were estimated to over $150 billion, and this explosion is expected to continue through the balance of this century. *See* McCray,

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[1]For a comprehensive analysis of the Court's decisions in this area and a description of its developing due process standards in the areas of personal and tax jurisdiction, *see* McCray, 1985 B.Y.U. L. Rev. 265.

Overturning Bellas Hess: Due Process Considerations, 1985 B.Y.U. L. Rev. at 265, n. 3. The rate of growth of mail order sales has been estimated at 8% to 12% per year. Advisory Committee on Intergovernmental Relations, *State and Local Taxation of Out-of-State Mail Order Sales,* 4 (April 1986).

Even more startling are the technological advances since *Bellas Hess* which are now available to mail order sellers and buyers. Advances in communication have been developed and widely accepted; "800" telephone numbers are now the functional equivalent of local phone numbers because no cost is charged to the buyer. The use of FAX machines for purchases is another post-*Bellas Hess* phenomenon.

To say that Folio derives no benefit from the state of Connecticut is to ignore the obvious. First and foremost, Folio enjoys a substantial and profitable economic market in its Connecticut customers – customers who, but for the lure of Folio, would probably have purchased their goods from in-state companies and paid a sales tax directly. Second, Folio depends upon the state of Connecticut to dispose of the millions of catalogs it sends into the state for its own benefit. The problems of garbage disposal and landfill overflow were not recognized at the time of *Bellas Hess* but are now major environmental concerns. Certainly, Folio's actions place a burden on the State which must be addressed.

Further, the Saks parent company derives a profit not only from Folio's Connecticut sales but also from Saks-Stamford's Connecticut sales. Under the holdings in *Nelson v. Montgomery Ward and Company, Inc.,* 312 U.S. 373 (1941), and *Nelson v. Sears, Roebuck & Co.,* 312 U.S. 359 (1941), if Saks-Stamford and Folio were part of one corporation, rather than a unitary enterprise of closely related corpora-

tions, Folio could be required to collect use taxes on its mail order sales even if they were unrelated to its store sales. See *National Geographic Society v. California Board of Equalization,* 430 U.S. 551 (1977). It seems to be denying reality to permit Saks to avoid this responsibility while still reaping the benefits by the device of creating a corporate enterprise with wholly-owned subsidiaries rather than one corporate entity.

In return for the benefits it receives, Folio is being asked not to *pay* a use tax but merely to *collect* one from Connecticut residents whose disposal of Folio catalogs costs the State money. The burden on Folio's interstate commerce centers primarily around the administrative requirements necessitated by collecting and forwarding the tax to Connecticut officials. However, what the *Bellas Hess* Court viewed in 1967 as "administrative and recordkeeping requirements [which] could entangle National's business in a virtual welter of complicated obligations to local jurisdiction," 386 U.S. at 759-60, are requirements very easily handled by relatively inexpensive computer hardware and software.

The intervening years have witnessed a most rapid development in the area of computer technology. The calculation of the various sales and use tax rates for each state, which would have been nearly impossible in 1967, can now, with available computer programs, be done cheaply, easily, and quickly. *See* Hartman, *Collection of the Use Tax on Out-of-State Mail-Order Sales,* 39 Vand. L. Rev. 993, 1011-12 (1986). Certainly, Folio, which is capable of targeting an estimated 20,000,000 catalogs a year nationally, Scroge, *Inside the Leading Mail Order Houses* (1989), now has the same ability to fulfill the use tax collection obligation as any other retailer. Any burden of compliance can now only be viewed

as minimal and not truly the burden to interstate commerce it once was.

This Connecticut case is one in a growing list of mail order sales and use tax cases being decided under or distinguished from *Bellas Hess*. The trial courts of Pennsylvania and North Dakota have held *Bellas Hess* as a total barrier to taxing out-of-state mail order sales, *L.L. Bean, Inc. v. Commonwealth Department of Revenue*, 101 Pa. Commw. 435, 516 A.2d 820 (1986); *Bloomingdale's By Mail, Ltd. v. Commonwealth Department of Revenue*, 130 Pa. Commw. 190, 567 A.2d 773 (1989); and *North Dakota v. Quill, Inc.*, No. 41677 (Dist. Ct. N.D. May 15, 1990) (*appeal pending*) App. p. A51, whereas the trial courts of Tennessee have sustained the constitutionality of sales and use tax collection obligations. Particularly noteworthy is that SFA Folio Collections, the Respondent here, was one of the parties in the Tennessee litigation. These cases distinguished *Bellas Hess* on the factual developments which have occurred since 1967. *SFA Folio Collections, Inc. v. Huddleston*, No. 89-3015-III (Ch. Tenn. March 11, 1991) App. p. A45, and *Bloomingdale's By Mail, Ltd. v. Huddleston*, No. 89-3017-II (Ch. Tenn. March 8, 1991) App. p. A40.

The *Bellas Hess* decision established a simple mechanical rule for state tax jurisdiction. This limited approach is similar in concept to the approach once espoused by this Court with regard to state corporation income/franchise taxes. In *Spector Motor Service v. O'Connor*, 340 U.S. 508 (1951), the Court held that a franchise tax measured by income cannot be validly applied to a corporation conducting interstate commerce even though the tax was nondiscriminatory and fairly apportioned. A similar tax, in economic terms, but one reworded with "magic words or labels"

In *Complete Auto Transit, Inc. v. Brady* 430 U.S. 247 (1978), a unanimous Court overruled *Spector*. The holding in *Spector* "deem[ed] irrelevant any consideration of the practical effect of the tax." *Id.* at 274. In place of a rule with "no relationship to economic realities," *id.* at 279, the Court established a comprehensive four-prong Commerce Clause analysis to be applied when interstate business is made the subject of a state tax.

Because of the enormity of the economic impact of mail order businesses on the individual states and the concomitant loss of tax revenue occasioned by sales to these businesses, the Petitioner ask this Court to reconsider *Bellas Hess* and modify its holding to reflect the economic and technological realities of the present day mail order market.

CONCLUSION

Doctrines which form the underpinning of the Commerce Clause have evolved in the last quarter of a century along with retailing practices and technology advances. The doctrine enunciated in *National Bellas Hess* in 1967 is today difficult to properly and realistically apply to mail order transactions in the 1990's and beyond. This Court is urged to grant the within petition and to address this important issue of state sales and use taxes which is developing into a clear divergence of holdings by the courts of the various states.

Respectfully submitted,
Petitioner

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SFA FOLIO COLLECTIONS, INC. *v.* TIMOTHY F. BANNON, COMMISSIONER OF REVENUE SERVICES (14023)

PETERS, C. J., SHEA, COVELLO, HULL and BORDEN, Js.

The plaintiff, F Co., a New York mail order company that is a wholly owned subsidiary of S Co., another New York corporation, which operates a store in Connecticut, appealed to the trial court from the assessment of sales and use tax liability by the defendant commissioner of revenue services. In assessing tax liability, the commissioner asserted that because F Co. mailed catalogs to Connecticut residents, maintained a toll-free "800" telephone number for customer use, placed advertising in magazines that ultimately reached Connecticut residents, and sent extra copies of catalogs to S Co.'s Connecticut store, F Co.'s business had a sufficient nexus with this state to justify the imposition of taxes. The commissioner further claimed that because F Co. is part of a larger enterprise of affiliated corporations, F Co. should be deemed to share the nexus that S Co. has with Connecticut. The trial court rendered judgment sustaining the plaintiff's appeal, from which the commissioner appealed. *Held*:

1. The trial court correctly determined that the imposition of sales and use taxes on F Co. was a violation of the due process and commerce clauses of the United States constitution because F Co. lacked sufficient nexus to this state, and that court's finding that F Co. and S Co. are separate and independently functioning corporate entities was not clearly erroneous.
2. The commissioner could not prevail on his claim that because commercial activity in a state is often sufficient for a state to assert personal

jurisdiction over an out-of-state company, such contact should be sufficient to support state taxation on an out-of-state mail order company, like F Co. whose only contacts with the state are through the United States mail and common carriers.

Argued November 8, 1990—decision released January 22, 1991

Appeal from the assessment of, inter alia, a sales and use tax liability against the plaintiff, brought to the Superior Court in the judicial district of Hartford-New Britain at Hartford and tried to the court, *Satter, J.*; judgment sustaining the plaintiff's appeal, from which the defendant appealed. *Affirmed.*

Richard K. Greenberg, assistant attorney general, with whom were *John G. Haines*, assistant attorney general, and, on the brief, *Clarine Nardi Riddle*, attorney general, and *Jane D. Comerford*, assistant attorney general, for the appellant (defendant).

Maryann B. Gall, with whom were *Laura A. Kulwicki* and *William H. Narwold*, for the appellee (plaintiff).

BORDEN, J. The issue in this tax appeal is whether the trial court correctly determined that the imposition of Connecticut sales and use taxes on the plaintiff, SFA Folio Collections, Inc. (Folio), a mail order company, was a violation of the due process and commerce clauses of the United States constitution because Folio lacks a sufficient nexus to the state. The defendant, the commissioner of revenue services (commissioner), assessed Folio with sales and use taxes pursuant to General Statutes § 12-406 et seq., asserting that a sufficient nexus between the state and Folio existed, primarily because Folio was part of an "enterprise" of other affiliated corporations, one of which, Saks Fifth Avenue Stamford, Inc. (Saks-Stamford), clearly had a taxable nexus to the state. We affirm the judgment of the trial court.

In February, 1987, the commissioner informed Folio that it was required to begin collection and remittance of sales and use taxes because it satisfied the definition of "[e]ngaged in business in the state" pursuant to General Statutes § 12-407 (15).[1] Folio had neither applied for a permit to collect such taxes in Connecticut, nor had it ever collected such taxes on its catalog sales to Connecticut residents. In justifying the imposition of the tax liability, the commissioner stated that "[t]he unitary nexus established from [Folio's] shared corporate name, logo, etc., with Saks Fifth Avenue-Stamford, Inc. is the basis of our position." The commissioner thereafter requested that Folio register with the department of revenue services and begin to collect the appropriate taxes on its catalog sales to Connecticut customers. Folio contested, as an unconstitutional application of Connecticut law, the imposition of a duty upon it to register pursuant to General Statutes § 12-411 (8).

The commissioner notified Folio that its registration application had been processed and its tax registration number assigned, although Folio had not applied for such a number. The commissioner then informed Folio

[1] General Statutes § 12-407 (15) provides: " 'Engaged in business in the state' means selling in this state, or any activity in this state in connection with selling in this state, tangible personal property for use, storage or consumption within the state or engaging in the transfer for a consideration of the occupancy of any room or rooms in a hotel or lodging house for a period of thirty consecutive calendar days or less, or rendering in this state any service described in any of the subdivisions of subsection (2) of this section. The term shall include but shall not be limited to the following acts or methods of transacting business: (a) Maintaining, occupying or using, permanently or temporarily, directly or indirectly, through a subsidiary or agent, by whatever name called, of any office, place of distribution, sales or sample room or place, warehouse or storage point or other place of business or (b) having any representative, agent, salesman, canvasser or solicitor operating in this state for the purpose of selling, delivering or taking orders."

that it would be issued an assessment of its tax liability. Thereafter, the commissioner imposed on Folio an assessment of $234,450.28, which comprised $163,052.71 in sales and use taxes, $55,072.25 in interest, and $16,305.32 in penalty costs. The commissioner later issued Folio an additional assessment of $20 for a sales and use tax license and permit.

Folio filed a petition for reassessment with the commissioner pursuant to General Statutes § 12-421, asserting that it was not "engaged in business" in Connecticut pursuant to § 12-407 (15), and, therefore, could not constitutionally be required to collect or to pay Connecticut sales and use taxes on its mail order sales to Connecticut residents. The commissioner denied Folio's appeal, and confirmed the assessment. Folio appealed the decision to the Superior Court pursuant to General Statutes § 12-422. The trial court reversed the decision of the commissioner, concluding that Folio did not have a sufficient nexus to Connecticut to sustain the imposition of a sales and use tax. The commissioner appealed to the Appellate Court, and we transferred the case to ourselves pursuant to Practice Book § 4023.

The facts stipulated by the parties may be summarized as follows. Folio, a wholly owned subsidiary of Saks & Company, conducts a nationwide mail order business. Both Folio and Saks & Company are New York corporations. Folio's principal place of business is in Yonkers, New York, and Saks & Company's corporate headquarters are in New York City. The two corporations share a number of common directors and officers, although each corporation maintains separate management for day-to-day operations. Additionally, Folio, with the consent of Saks & Company, maintains as part of its corporate name the "SFA" registered trademark of "Saks Fifth Avenue." This trademark, which often appears in Folio's catalogs, characterizes

the high quality of merchandise and service traditionally associated with Saks & Company. To the extent that a customer associates "SFA" with Saks Fifth Avenue, Folio is benefited.

Saks & Company, in addition to owning Folio, owns Saks-Stamford, a separate corporation that operates a retail store in Stamford, Connecticut. Folio and all Saks Fifth Avenue retail stores, including Saks-Stamford, share sales and financial data and profit and loss statements. The management groups for Folio and Saks-Stamford, however, are separate and operate autonomously. Although the corporations are independent, Folio does, through its printers,[2] send extra copies of its mail order catalog by common carrier to the Saks-Stamford general manager in order to inform store employees of fashion trends, to be used as reference guides, and to serve as merchandise educational tools. Folio customers may also use Saks-Stamford's tailoring services for a standard fee, but these services are also available to the public at large regardless of where an item was purchased. Folio sells some of the same items that are available at Saks-Stamford, but many of these items are also available at other retail stores throughout the country.

In conducting its business, Folio distributes mail order catalogs[3] and flyers to Connecticut residents and receives orders either by mail or by telephone. Customers pay for their orders by credit card or check,[4]

[2] Folio's printers are located outside of Connecticut.

[3] Folio does not design, prepare, print, publish or mail its catalogs in or from Connecticut.

[4] Folio does not fill any order that is paid by check until the check has been cleared by the bank, thereby eliminating the need to use the Connecticut court system in order to collect bad debts. Additionally, Folio does not bear the risk of loss for any purchases by credit card, as such risk falls upon the credit card company, further eliminating any claim that Folio derives benefits from the Connecticut court system.

and Folio fills them in Yonkers, New York. Customers may use their Saks & Company charge card when making purchases from Folio, as well as when buying items at Saks-Stamford. Folio often includes advertising for Folio in the form of "bill inserts" in the charge card bill received by the customer from Saks & Company. Folio does, however, pay for the customer's return envelope accompanying the billing statement. Folio delivers purchases to Connecticut buyers either through the mails or by common carrier, with the customers paying for the shipping, handling, and transportation of their orders. Folio refers its customers to its Yonkers office for customer assistance, merchandise return or exchange, and other services.

Folio does not operate retail stores, and does not maintain under its corporate name any store, office, distribution house, sales house, sample room, warehouse, or other place of business in Connecticut. Folio does not have any solicitors, canvassers, sales persons, authorized agents, or representatives in Connecticut. Folio is not licensed to do business in Connecticut, and has no inventory or merchandise in the state. Folio does not maintain a phone number in Connecticut; all customer contact is through the use of a toll free "800" number. Folio has no bank accounts in Connecticut, does not retain security interests in any goods sold to Connecticut residents, and does not investigate credit or collect accounts in Connecticut.

The commissioner first claims that the trial court incorrectly determined that there was such an absence of the requisite nexus between Folio and Connecticut that the imposition of the sales and use taxes violated the due process and commerce clauses of the federal constitution. While the commissioner asserts that Folio, independently, has a sufficient nexus to Connecticut, his primary claim in this regard is that, under an enter-

prise theory, the presence in Connecticut of an affiliated corporation, namely, Saks-Stamford, supplies Folio with a sufficient nexus to sustain the imposition of sales and use taxes. Secondly, the commissioner claims that, in light of the developments in "the judicial analysis of due process and the mail-order industry," the due process standard applicable to personal jurisdiction claims should be employed so that an "economic presence" in Connecticut satisfies the nexus requirement for state taxation. We disagree.

I

This appeal is governed by the United States Supreme Court decision in *National Bellas Hess, Inc.* v. *Department of Revenue*, 386 U.S. 753, 87 S. Ct. 1389, 18 L. Ed. 2d 505 (1967), and our recent decision in *Cally Curtis Co.* v. *Groppo*, 214 Conn. 292, 572 A.2d 302, cert. denied, U.S. , 111 S. Ct. 77, 112 L. Ed. 2d 50 (1990). In *National Bellas Hess, Inc.*, the United States Supreme Court determined that constitutional constraints limit the authority of a state to impose sales and use tax liability upon an out-of-state seller. *National Bellas Hess, Inc.* v. *Department of Revenue*, supra, 756; *Cally Curtis Co.* v. *Groppo*, supra, 297. "Such a collection burden when placed upon an out-of-state seller triggers due process concerns as well as imposes a restraint upon interstate commerce." *Cally Curtis Co.*, v. *Groppo*, supra; see also *National Bellas Hess, Inc.* v. *Department of Revenue*, supra; *L.L. Bean, Inc.* v. *Department of Revenue*, 516 A.2d 820, 824 (Pa. Commw. 1986). In *Cally Curtis Co.*, we reaffirmed the applicability of *National Bellas Hess, Inc.*, to a claim of taxability like that asserted in this case, and held that where the only nexus between Connecticut and the corporation was the in-state presence for three days of video tapes leased by the out-of-state corporation to its in-state customers, an insufficient nexus existed to warrant the imposition of the Connecticut use tax. *Cally Curtis Co.* v. *Groppo*, supra, 301.

In determining whether a state tax conforms with constitutional due process requirements, the United States Supreme Court has held that the " 'simple but controlling question is whether the state has given anything for which it can ask return. " *National Bellas Hess, Inc.* v. *Department of Revenue*, supra, quoting *Wisconsin* v. *J. C. Penney Co.*, 311 U.S. 435, 444, 61 S. Ct. 246, 85 L. Ed. 267 (1940). Because Congress has the exclusive authority to regulate interstate commerce, " '[s]tate taxation falling on interstate commerce. . . can only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys.' " *National Bellas Hess, Inc.* v. *Department of Revenue*, supra, 756, quoting *Freeman* v. *Hewit*, 329 U.S. 249, 253, 67 S. Ct. 274, 91 L. Ed. 265 (1946); see also *Cally Curtis Co.* v. *Groppo*, supra, 298. Therefore, the relevant legal inquiry in reviewing the constitutionality of imposing the duty of collection of such a tax upon an out-of-state seller is whether there exists " 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.' " *National Bellas Hess, Inc.* v. *Department of Revenue*, supra, quoting *Miller Bros. Co.* v. *Maryland*, 347 U.S. 340, 344–45, 74 S. Ct. 535, 98 L. Ed. 744 (1954); see also *Cally Curtis Co.* v. *Groppo*, supra. "The existence of such a link or nexus will turn upon the individual facts of each case." *Cally Curtis Co.* v. *Groppo*, supra.

At the outset, the commissioner claims that Folio's contacts with Connecticut are greater than those of the taxpayers in *National Bellas Hess, Inc.*, and *Cally Curtis Co.* These alleged contacts consist of the large number of catalogs Folio mails to Connecticut residents,[5]

[5] Folio mailed to Connecticut residents 649,000 catalogs in 1986 and 733,000 catalogs in 1987.

the operation of a toll-free "800" number for customer use, the placement of advertisements in magazines that ultimately reach Connecticut residents, and the extra copies of its catalogs that Folio sends to Saks-Stamford's general manager for business use. The trial court, in examining this claim of nexus, however, found "the facts of *National Bellas Hess, Inc.*, and *Cally Curtis Co.* indistinguishable from the facts of this case."

In reviewing the trial court's determination, in this context, "the effect of admitted facts is a question of law." *Nelson* v. *Montgomery Ward & Co.*, 312 U.S. 373, 376, 61 S. Ct. 593, 85 L. Ed 897 (1941). Therefore, the relevant inquiry is whether any of the asserted contacts establish some definite link or some minimum connection between Folio and Connecticut. *National Bellas Hess, Inc.* v. *Department of Revenue*, supra.

The commissioner's claim of nexus based upon the catalogs ignores the fact that the catalogs, once delivered to Connecticut residents, are the property of the residents, not Folio.[6] Such activity, therefore, does not establish a taxable link between Folio and the state. The use of a toll-free "800" number for Connecticut residents to place orders likewise does not demonstrate a sufficient link to Connecticut. *L.L. Bean, Inc.* v. *Department of Revenue*, supra, 825. Additionally, the advertisements for Folio that appear in magazines are not created or placed in magazines in Connecticut. The fact that the magazines eventually are sold in Connecticut does not establish a nexus between Folio and the state. Finally, the catalogs sent by Folio's printers to Saks- Stamford do not establish a link to Connecticut because these catalogs are used for employee training

[6] The commissioner's argument that Folio derives benefit from Connecticut by virtue of the state disposing of the catalogs as paper trash is likewise without merit. Because the catalogs are the property of the Connecticut residents, it is axiomatic that it is the resident who is deriving the benefit from the state and who must contribute to the cost of the disposal.

and reference purposes, not for the purpose of having the Saks-Stamford employees solicit Folio sales from Connecticut residents. Compare *Scripto, Inc.* v. *Carson*, 362 U.S. 207, 80 S. Ct. 619, 4 L. Ed. 2d 660 (1960).

On the facts of this case, we can discern no greater nexus between Connecticut and Folio than existed between Connecticut and the out-of-state corporation in *Cally Curtis Co.* We conclude, therefore, that Folio, viewed independently, does not have a nexus to Connecticut sufficient to support the imposition of sales and use taxes.

We turn, therefore, to the commissioner's primary claim, namely, that because Folio is part of a larger enterprise of affiliated corporations, Folio should be deemed to share the nexus that Saks-Stamford has with Connecticut. We are not persuaded.

The parties do not contest that Saks-Stamford is a Connecticut corporation responsible for paying Connecticut sales and use taxes because it has local retail stores in the state. *Nelson* v. *Sears, Roebuck & Co.*, 312 U.S. 359, 61 S. Ct. 586, 85 L. Ed. 888 (1941). The parties disagree, however, about the implications to be drawn from the connections between these affiliated but independent corporations when the issue is the sufficiency of Folio's nexus to Connecticut for sales and use tax purposes.

Significantly, the commissioner does not assert that we should find a nexus pursuant to a "piercing the corporate veil"[7] or "alter ego"[8] theory. The commissioner

[7] The disregard of a technically correct corporation "in terms of a metaphor, is often called 'piercing the corporate veil.' " H. Henn & J. Alexander, Laws of Corporations (3d Ed. 1983) § 146, p. 344. "The concept [of corporateness] will be sustained only so long as it is invoked and employed for legitimate purposes. Perversion of the concept to improper uses and dishonest ends (e.g., to perpetuate fraud, to evade the law, to escape obligations), on the other hand, will not be countenanced." Id., § 146, p. 346.

[8] "A conventional statement of [the 'alter ego' doctrine] declares that 'piercing the veil' is proper when (1) such unity of ownership and interest

does not dispute the trial court's factual finding that the Folio and Saks-Stamford are "distinct corporate entities." Rather, the commissioner claims that because these separate entities are linked by their common corporate parent, Saks & Company, their separate corporate existence should be disregarded and they should be treated as one enterprise for the purposes of establishing a nexus for taxation.[9] Should such a determination be made, Folio would be subject to sales and use tax liability, despite the lack of an independent nexus with Connecticut, because it would be "plainly accorded the protection and services of the taxing State"; *National Bellas Hess, Inc.* v. *Department of Revenue*, supra, 757; as a result of the presence of the Saks-Stamford retail store in Connecticut *Nelson* v. *Montgomery Ward & Co.*, supra; *Nelson* v. *Sears, Roebuck & Co.*, supra.

It is undisputed that in Connecticut a court will disregard the corporate structure and pierce the corporate veil " 'only under exceptional circumstances, for example, where the corporation is a mere shell, serving no legitimate purpose, and used primarily as an intermediary to perpetuate fraud or promote injustice.' " *Angelo Tomasso, Inc.* v. *Armor Construction & Paving, Inc.*,

exists that the two affiliated corporations have ceased to be separate and the subsidiary has been relegated to the status of the 'alter ego' of the parent; and (2) where recognition of them as separate entities would sanction fraud or lead to an inequitable result." P. Blumberg, The Law of Corporate Groups, Statutory Law-General (1987) § 2.02.2, p. 37.

[9] "Traditionally, the law has viewed each corporation as a separate legal entity, with separate rights and obligations. For legal purposes, a bright line of distinction was drawn between the corporation and its shareholders." P. Blumberg, The Law of Corporate Groups, Procedural Law (1983) § 1.01.1, p. 1. The "[e]ntity theory" of corporate law is the premise "that a corporation is a fictitious, artificial, legal person or juristic entity . . . . [On the other hand,] [t]he 'enterprise theory' stresses the underlying commercial enterprise, without emphasis on the entity-aggregate distinction of the components." H. Henn & J. Alexander, Laws of Corporations (3d Ed. 1983) § 78, pp. 145-46.

187 Conn. 544, 557, 447 A.2d 406 (1982). Nevertheless, the commissioner seeks to have this court abandon our traditional notions of corporate law and ignore Folio's separate corporate existence under an enterprise theory. In support of this legal proposition, the commissioner relies on three authorities: (1) the "unitary business" principle articulated in *Container Corporation of America* v. *Franchise Tax Board*, 463 U.S. 159, 103 S. Ct. 2933, 77 L. Ed. 2d 545, reh. denied, 464 U.S. 909, 104 S. Ct. 265, 78 L. Ed. 2d 248 (1983); (2) Dean Phillip I. Blumberg's four volume treatise, The Law of Corporate Groups; and (3) the Connecticut Superior Court case of *Hartford Steam Services Co.* v. *Sullivan*, 26 Conn. Sup. 277, 220 A.2d 772 (1966).

First, the commissioner cites *Container Corporation of America* v. *Franchise Tax Board*, supra, as support for the proposition that "[w]here a group of corporations are formed and operated as a unitary enterprise, there is no constitutional barrier to the group being viewed as a unitary enterprise and taxed as such." The commissioner fails to recognize, however, that the "unitary business principle" is a statutorily created system of calculating corporate income tax "by first defining the scope of the 'unitary business' of which the taxed enterprise's activities in the taxing jurisdiction form one part, and then apportioning the total income of that unitary business between the taxing jurisdiction and the rest of the world on the basis of a formula taking into account objective measures of the corporation's activities within and without the jurisdiction." Id., 165. Clearly, there is no statute within the Connecticut sales and use tax chapter; General Statutes § 12-406 et seq.; that allows the commissioner to treat separate corporations as part of one enterprise for the purpose of imposing sales and use tax liability, and the commissioner does not make such a claim. Absent such statu-

tory authority, the line of cases pursuant to the "unitary business principle" are inapplicable.

Second, the commissioner cites as support for the enterprise theory Dean Phillip I. Blumberg's four volume treatise on The Law of Corporate Groups, supra. Without determining whether the commissioner's general reference to the multivolume treatise constitutes adequate briefing of the issue, we find no legal support therein for the commissioner's conclusion that "[s]imply stated, the fact that the Saks-Stamford store and Folio are wholly-owned affiliated corporations rather than divisions of the same corporation is without constitutional significance and not controlling."

To the contrary, it is a fundamental principle of corporate law that "the parent corporation and its subsidiary are treated as separate and distinct legal persons even though the parent owns all the shares in the subsidiary and the two enterprises have identical directors and officers. Such control, after all, is no more than a normal consequence of controlling share ownership." H. Henn & J. Alexander, Laws of Corporations (3d Ed. 1983) § 148, p. 355. Furthermore, the separate corporate entities or personalities of affiliated corporations will be recognized, absent illegitimate purposes, unless: "(a) the business transactions, property, employees, bank and other accounts and records are intermingled; (b) the formalities of separate corporate procedures for each corporation are not observed . . . (c) the corporation is inadequately financed as a separate unit from the point of view of meeting its normal obligations . . . (d) the respective enterprises are not held out to the public as separate enterprises; (e) the policies of the corporation are not directed to its own interests primarily but rather to those of the other cor-

poration." H. Henn & J. Alexander, supra, § 149, pp. 355–56; see also *Hammond* v. *United States*, 764 F.2d 88, 100 (2d Cir. 1985).[10]

This is not a situation where the corporate assets have been intermingled, where the formalities of separate corporate procedure have been ignored, or where the corporation is inadequately financed. Additionally, as determined by the trial court,[11] the corporations are

[10] In *Hammond* v. *United States*, 764 F.2d 88, 100 (2d Cir. 1988), the Court of Appeals for the Second Circuit, in reviewing a decision of the United States District Court for the District of Connecticut, noted that "at times, both state law and the [Internal Revenue Code] abandon the notion of the separate identity of corporations for narrow purposes and in limited situations[;] see, e.g. *United States* v. *Reading Co.*, 253 U.S. 26, 62–63, 40 S. Ct. 425, 434, 64 L. Ed. 760 (1920) (where subsidiary is mere agent or instrumentality of parent, separate corporate existence of subsidiary may be ignored); *Weisser* v. *Mursam Shoe Corp.*, 127 F.2d 344, 348 (2d Cir. 1942) (same); N.Y. Bus. Corp. Law § 630 (McKinney 1963) (largest shareholders liable for wage debt of insolvent corporations); IRC § 951(a), 26 U.S.C. § 951(a) (1982) (income of controlled foreign corporation deemed to be income of corporation's shareholder); IRC § 481, 26 U.S.C. 481 (1982) (authorizing IRS to reallocate income among commonly-held businesses so as to prevent tax evasion). . . ." Similarly, the Court of Appeals for the Tenth Circuit has recently held that "[w]e believe that the separate treatment for tax purposes of parent and wholly-owned subsidiary should not be extended when we can see no business purpose beyond an opportunity to manipulate for tax purposes." *Marathon Oil Co.* v. *Commissioner of Internal Revenue*, 838 F.2d 1114, 1120 (10th Cir. 1987).

While these decisions are not binding precedent on this court, *Hammond* and *Marathon Oil Co.* lend further support to our conclusion that it is not the place of this court to ignore the separate entity of a corporation absent a fraudulent, evasive, or manipulative purpose in forming or maintaining the corporation. The commissioner has made no claim that Folio was incorporated or maintained for the purpose of evading sales and use taxes, and no such claim would be credible based upon the evidence presented at trial. Compare *Hartford Steam Services Co.* v. *Sullivan*, 26 Conn. Sup. 277, 220 A.2d 772 (1966) (subsidiary mere paper corporation).

[11] The trial court concluded that "[a]lthough [Folio and Saks-Stamford] have some common directors and officers, are affiliates of the same parent company, use the same trademarks and logos, sell similar merchandise and share financial and market information, they are distinct corporate entities. Saks-Stamford is not Folio's retail store, agent instrumentality, or alter ego. The finding of the Commissioner's unit chief that Folio is

not held out to the public as one entity. Because we conclude that the finding of fact that Folio is a separate corporate entity was not clearly erroneous; *French* v. *Clinton*, 215 Conn. 197, 205, 575 A.2d 686 (1990); we would not be justified in disregarding Folio's separate identity for tax purposes. *Angelo Tomasso, Inc.* v. *Armor Construction & Paving, Inc.*, supra, 557.

In further support of his contention that this court should apply an economic enterprise theory, the commissioner argues that if we recognize a constitutional distinction between affiliated corporations, such as in this case, and divisions of the same company; *Nelson* v. *Sears, Roebuck & Co.*, supra; the result would be that "any retailer with an out-of-state mail order component could avoid collecting sales and use tax simply by separately incorporating the retail and mail order businesses." While we agree with the commissioner's assertion, we conclude that it does not support his claim for rejecting Folio's corporate entity and applying the enterprise theory.

The commissioner's argument demonstrates a misunderstanding of a fundamental principle underlying our system of taxation, namely, that " 'taxpayers may arrange their affairs to minimize their tax liabilities. Unlike tax evasion, tax avoidance through careful planning of both transactions and corporate structure is a legitimate right of every taxpayer.' " Jurinski, "Agency Relationships in Determining Nexus: Groping for a Solution," 7 Journal of Taxation 321, 321 (1989). Furthermore, the commissioner ignores the fact that a business that is incorporated separately from a parent or affiliated corporation incurs additional burdens by the very fact of its separate corporate existence. Indeed,

engaged in business in Connecticut because a 'unitary nexus' was established by its 'shared corporate name, logo, etc., with Saks Fifth Avenue Stamford Inc.' has no basis in the evidence or the law."

as Folio argues, because of its separate corporate existence it must register with the secretary of the state, qualify to do business, hold a corporate charter, issue stock, maintain corporate minute books, file corporate income tax returns, and remit payroll and unemployment taxes. Folio is also subject to suit for contractual and other obligations that stem from the conduct of its business. Even as a part of a deliberate tax-avoidance strategy, the fact that Folio is incorporated as an entity separate from Saks-Stamford and Saks & Company does not, standing alone, permit a taxing authority to disregard Folio's corporate identity.

The commissioner also relies upon the decision of the Superior Court in *Hartford Steam Services Co.* v. *Sullivan*, supra, to support the application of the enterprise theory to Folio for state tax purposes. In describing the economic enterprise theory, the court, *Parskey, J.*, stated that "[t]his is not the negative concept variously described as 'piercing the corporate veil' or 'disregarding the corporate fiction,' a concept based on equitable principles and designed to frustrate fraud, misrepresentation or illegality. It is, rather, a positive principle, the effect of which is to remove judicial blinders so as to enable the court to see things as they really are." Id., 281. Thus, "where the economic enterprise is one, the corporate forms being largely paper arrangements that do not reflect the business realities, the court should deal with the realities." Id. That case is neither controlling on us nor persuasive because here, unlike the facts of that case, the business reality is that Folio is not a paper arrangement but a separate and independently functioning corporation.

II

The commissioner's second claim is that, in light of developments in due process analysis and in the mail-order industry, the nexus requirement of the due pro-

cess clause is satisfied where an out-of-state corporation, such as Folio, has an "economic presence" in the state. This argument, at its roots, seeks to adopt the minimum contacts standard of personal jurisdiction analysis for state taxation on an out-of-state mail order company by dispelling the need for the company to have some physical connection[12] with the state beyond the use of the United States mail or a common carrier. We decline to adopt such an analysis.

The commissioner bases his argument on developments in due process case law for personal jurisdiction

[12] A review of Supreme Court case law in the area of state imposition of sales and use taxes demonstrates that some degree of physical presence, whether by the presence of a retail store, offices, local agents, solicitors, or local advertising, is constitutionally required to support such a burden: " 'Case law has established that a sufficient nexus is found to exist where local agents of the seller are present in the taxing state. *Felt & Tarant Manufacturing Co.* v. *Gallagher*, 306 U.S. 62, 59 S. Ct. 376, 83 L. Ed. 488 (1939); *General Trading Co.* v. *State Tax Commission of the State of Iowa*, 322 U.S. 335, 64 S. Ct. 1028, 88 L. Ed. 1309 (1944). A similar result has been reached where the seller has local retail stores which are present in the taxing state. *Nelson* v. *Sears, Roebuck & Co.*, 312 U.S. 359, 61 S. Ct. 586, 85 L. Ed. 888 (1941) . . . . And in *National Geographic Society* [v. *California Equalization Board*, 430 U.S. 551, 97 S. Ct. 1386, 51 L. Ed. 2d 631 (1977)], the presence in the taxing state of two offices which solicited advertisements and received the benefit of municipal protection (fire, police, etc.) was held a sufficient nexus.' " *Cally Curtis Co.* v. *Groppo*, 214 Conn. 292, 298-99, 572 A.2d 302 (1990) quoting *L.L. Bean, Inc.* v. *Department of Revenue*, 516 A.2d 820, 824-25 (Pa. Commw. 1986).

"In *Miller Brothers Co.* v. *Maryland*, [347 U.S. 340, 74 S. Ct. 535, 98 L. Ed. 744 (1954)] however, the United States Supreme Court held that Maryland 'could not constitutionally impose upon a Delaware seller an obligation to collect use taxes where the Delaware firm had no retail outlets or sales solicitors in Maryland, despite the presence of advertising in Maryland which resulted in substantial sales and the delivery of goods into Maryland by the seller using its own trucks and drivers.' *L.L. Bean, Inc.* v. *Department of Revenue*, supra, 825. Furthermore, in *National Bellas Hess, Inc.* v. *Department of Revenue*, [386 U.S. 753, 87 S. Ct. 1389, 18 L. Ed. 2d 505 (1967)] the United States Supreme Court found an insufficient nexus where the only contacts between the seller and the taxing state were through the United States mail or common carrier." *Cally Curtis Co.* v. *Groppo*, supra, 299.

purposes, claiming that because commercial activity in a state is often sufficient for a state to exert personal jurisdiction over an out-of-state company; *Asahi Metal Industry Co.* v. *Superior Court of California*, 480 U.S. 102, 112, 107 S. Ct. 1026, 94 L. Ed. 2d. 92 (1987); such contacts should be sufficient to support state taxation on an out-of-state mail order company whose only contacts with the state are through the United States mail and common carriers.[13] The commissioner ignores, however, the general principle that "[i]t is the nature of the state's action that determines the kind and degree of activity in the state necessary for satisfying the requirements of due process." *Travelers Health Assn.* v. *Virginia*, 339 U.S. 643, 653, 70 S. Ct. 927, 94 L. Ed. 1154 (1949) (Douglas, J., concurring); see also *Kulick* v. *Department of Revenue*, 624 P.2d 93, 97 (Or.

[13] The commissioner asserts that more recent case law has focused on the "totality [of circumstances] of the business activities in a particular state" in determining whether a nexus exists to support state taxation. The cases cited, however, do not support the commissioner's argument that minimum contacts or economic presence alone should be the applicable standard.

In *National Geographic Society* v. *California Board of Equalization*, 430 U.S. 551, 97 S. Ct. 1386, 51 L. Ed. 2d 631 (1977), the United States Supreme Court upheld the imposition of sales and use taxes where the corporation had present in the taxing state two offices that solicited advertisements and received the benefit of municipal protection. Likewise, in *Reader's Digest Assn.* v. *Mahin*, 44 Ill. 2d 354, 255 N.E.2d 458 (1970), the Illinois Supreme Court upheld the imposition of sales and use taxes because the corporation used local advertising and resident solicitors. In *Cooey-Bentz Co.* v. *Lindley*, 66 Ohio St. 2d 54, 419 N.E.2d 1087 (1981), the court cited advertising directed at Ohio residents, as well as deliveries, installations, and repairs made in Ohio by the defendant West Virginia retailer to justify applying a use tax. Lastly, in *Franklin Mint Co.* v. *Tully*, 94 App. Div. 2d 877, 463 N.Y.S.2d 566 (1983), aff'd, 61 N.Y.2d 980, 463 N.E.2d 621, 475 N.Y.S.2d 280 (1984), the corporation engaged in local advertising, as well as delivery, installation, and service of goods located in New York.

A review of these cases demonstrates that a degree of physical connection to the taxing state, beyond the use of the mails or common carrier, existed in each case. In this case, Folio did not engage in any local advertising or local delivery, servicing or installation as part of its own corporate activities.

1981). The degree of due process required for exercising personal jurisdiction is not necessarily the same as that required to justify a state tax on an out-of-state seller. *Kulick* v. *Department of Revenue*, supra.[14]

Indeed, in *National Bellas Hess, Inc.* v. *Department of Revenue*, supra, 758, the Supreme Court explicitly recognized that a "sharp distinction" exists "between mail order sellers with retail outlets, solicitors, or property within a State, and those who do no more than communicate with customers in the State by mail or common carrier as part of a general interstate business." The commissioner's claim ignores the interests of the commerce clause, specifically discussed in *National Bellas Hess, Inc.* v. *Department of Revenue*, supra, which provide that " 'state taxation falling on interstate commerce . . . can only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys.' " Id., 756, quoting *Freeman* v. *Hewit*, 329 U.S. 249, 253, 67 S. Ct. 274, 91 L. Ed. 265 (1946). The commissioner's bald assertion that "Folio has purposely availed itself of the privilege of conducting activities in Connecticut, thus invoking the benefits and protection of its laws," fails to clarify *how* Folio is benefitted

[14] In *Kulick* v. *Department of Revenue*, 624 P.2d 93, 97 (Or. 1981), the Oregon Supreme Court analyzed the applicability of the minimum contacts standard to a case involving a challenge to the imposition of a tax on nonresident shareholders of a Subchapter S corporation. That court noted that "[w]hen [the assertion of personal] jurisdiction is challenged, the due process issue concerns not the nonresident's substantive obligation, which theoretically should be the same in whatever court tries the case, but rather the legitimacy of that state's putting the nonresident to the inconvenience, the possible procedural drawbacks, and the judgment of what is asserted to be an inappropriate forum. A tax law, by contrast, is addressed to a general class of persons on whom the state means to place the substantive obligation to contribute to its revenues. It is not at all clear that the 'contacts' that due process demands for the first purpose are identical with the 'nexus' required for the second."

by local government when its contacts to Connecticut are solely through the United States mail and common carriers. Compare *D.H. Holmes Co. Ltd.* v. *McNamara*, 486 U.S. 24, 108 S. Ct. 1619, 100 L. Ed. 2d 21 (1988) (presence of retail stores in state); *National Geographic Society* v. *California Board of Equalization*, 430 U.S. 359, 97 S. Ct. 1386, 51 L. Ed 2d 631 (1977) (presence of two offices that solicited advertisements in state); *Scripto, Inc.* v. *Carson*, 362 U.S. 207, 80 S. Ct. 619, 4 L. Ed. 2d 660 (1959) (presence of solicitors in state).

The commissioner's argument that we should adopt an "economic presence" analysis in essence parallels the reasoning of the dissent in *National Bellas Hess, Inc.* v. *Department of Revenue*, supra. Justice Fortas argued that the imposition of the sales and use tax on the mail order company was proper, stating that "large-scale, systematic continuous solicitation and exploitation of the Illinois consumer market is a sufficient 'nexus' to require Bellas Hess to collect from Illinois customers . . . ." Id., 761. Furthermore, Justice Fortas would have found sufficient nexus to support the application of a tax where *National Bellas Hess, Inc.*, "regularly and continuously engaged in 'exploitation of the consumer market' . . . by soliciting residents of Illinois who live and work there and have homes and banking connections there . . . ." Id., 762. This view, however, has not been adopted by the Supreme Court, despite its recent review of the issue in *D.H. Holmes Co. Ltd.* v. *McNamara*, supra. In that case, the United States Supreme Court reaffirmed its adherence to *National Bellas Hess, Inc.*, and to the rule of constitutional law that a state may not collect sales and use taxes from a mail order company where its only contacts are through the mail or common carriers. We therefore reject the commissioner's claim that would have us dispense with the constitutional safeguards of

NO. CV 87-0338611 S
SFA FOLIO COLLECTIONS, INC. : SUPERIOR COURT
: JUDICIAL DISTRICT OF
v. HARTFORD-NEW BRITAIN
AT HARTFORD

TIMOTHY F. BANNON, COMMISSIONER : APRIL 2, 1990
OF DEPARTMENT OF REVENUE SERVICES
OF THE STATE OF CONNECTICUT

MEMORANDUM OF DECISION

The plaintiff SFA Folio Collections, Inc. (hereinafter Folio) appeals from decisions of the defendant Commissioner of the Department of Revenue Services (hereinafter Commissioner) assessing Folio with a sales and use tax liability of $234,450.28, including interest and penalty, and with a sales and use tax license fee of $20.00. Folio asserts that such assessments violate the Commerce Clause (Article I, Section 8, Clause 3) and the Due Process Clause (14th Amendment) of the United States Constitution.

The parties have stipulated to the following facts: Folio is a New York corporation having its principal place of business in Yonkers, New York. It engages in a mail order catalog business from its Yonkers location, selling high quality merchandise. Written or telephone purchase orders from persons throughout the United States, including Connecticut, are received in Yonkers and merchandise to fill the orders is shipped from Yonkers by common carrier or United States mail. Folio has no retail stores anywhere, and specifically in Connecticut does not have any store, office, distribution center or other facility, maintain any stock of goods or inventory, or employ any solicitors, canvassers or sales people. It has no Connecticut telephone directory

listing, retains no security interest in goods sold to Connecticut residents, does no credit investigation or collections in Connecticut, has no Connecticut bank accounts and does no repair or servicing of merchandise in Connecticut. It sent to Connecticut residents in 1986 649,000 catalogs and in 1987 733,000 catalogs, realizing sales revenues in those years in excess of $2,000,000.

Folio catalogs refer customers to its offices in Yonkers for customer assistance, merchandise return or exchange, and all other services.

Folio is a wholly-owned subsidiary of Saks and Company, a New York corporation with corporate headquarters in New York City. The Chairman and Chief Executive Officer of Saks and Company is a director of Folio and two other officers of Saks and Company are officers of Folio.

Saks Fifth Avenue of Stamford, Inc. (hereinafter Saks-Stamford) is a Connecticut corporation which operates a retail store in Stamford, Connecticut. It is also a wholly-owned subsidiary of Saks and Company and has some common officers and directors with Folio. The day-to-day operations of Saks-Stamford and Folio are each conducted by separate management groups and neither group makes decisions for the other corporation.

Saks-Stamford sells some merchandise identical to that sold by Folio. Folio customers can choose to use the tailoring services of Saks-Stamford, which services are available to anyone, and Folio customers are charged standard fees.

"SFA" (an abbreviation for Saks Fifth Avenue) and "Saks Fifth Avenue" are registered trademarks used in the Folio catalogs and the Saks-Stamford store, and Folio and Saks-

Stamford, along with all affiliates of Saks and Company, share a great variety of sales information, financial data and profit and loss statements.

In February 1987 a unit chief of the department of revenue services informed Folio that it was "engaged in business as described in Section 12-407(15) of the Connecticut Statutes. The unitary nexus established from your shared corporate name, logo, etc., with Saks Fifth Avenue-Stamford, Inc. is the basis of our position." Folio was asked to register with the department and charge a Connecticut sales tax on its sales to Connecticut residents. When Folio refused, on July 1, 1987 the Commissioner assessed a sales and use tax liability of $234,450, including penalty and interest to that date, and imposed a $20 sales and use tax license fee.[1] Folio petitioned for reassessment. The Commissioner denied Folio's petition on October 23, 1987 and Folio then appealed to this court pursuant to § 12-422.

The central question in this appeal is the precedential weight to be given to *National Bellas Hess v. Department of Revenue*, 386 U.S. 753 (1967). That case squarely holds that a state may not impose on an out-of-state mail order company the duty to collect a use tax on purchases by its residents when the company's only contact with the state's residents is by common carrier or the United States Mail. 386 U.S. at 758. See *D. H. Holmes Company, Ltd. v. McNamara*, 486 U.S. 24, 33 (1988). Folio relies on *National Bellas Hess* to sustain its appeal to the Commissioner's assessment of use taxes.

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[1]Since the assessment, General Statutes § 12-407(12) has been amended by Public Act 89-41 to define retailers subject to use taxes to include mail order businesses.

The Commissioner seeks to distinguish *National Bellas Hess* on the grounds that Folio has substantially more contacts with Connecticut than National Bellas Hess had with Illinois. He points to Folio sending 649,000 catalogs to Connecticut residents in 1986 and 733,000 in 1987, maintaining a toll-free "800" telephone number for Connecticut customers to place orders with Folio's Yonkers' office, shipping extra copies of its catalogs to Saks-Stamford, and Folio's customers getting tailoring services at Saks-Stamford. The tailoring service is made available by Saks-Stamford to all customers. Taking together, all of these contacts do not create the necessary nexus required by *National Bellas Hess.*

The Commissioner's main assertion is that the Saks-Stamford store is a retail outlet of Folio which brings the case within the ambit of *Nelson v. Sears, Roebuck & Co.,* 312 U.S. 359 (1941), *Nelson v. Montgomery Ward & Company, Inc.,* 312 U.S. 373 (1941), and *National Geographic Society v. California Board of Equalization,* 430 U.S. 551 (1977). In those cases, the mail order company maintained a retail store or office in the taxing state which the Court held entitled the state to require collection of use taxes on the company's mail order sales. In this case, however, Folio and Saks-Stamford are separate corporations. Although they have some common directors and officers, are affiliates of the same parent company, use the same trademarks and logos, sell similar merchandise and share financial and market information, they are distinct corporate entities. Saks-Stamford is not Folio's retail store, agent, instrumentality, or alter ego. The finding of the Commissioner's unit chief that Folio is engaged in business in Connecticut because a "unitary nexus" was established by its "shared corporate name, logo, etc., with Saks Fifth Avenue Stamford, Inc." has no basis in the evidence or in the law.

The Commissioner's second argument is that this Court should find the requisite nexus by reason of Folio's "economic presence" in Connecticut.[2] Recognizing that *National Bellas Hess* and its line of cases predicated the constitutional basis for imposition of state use taxes upon an out-of-state mail order company having some physical presence, either property, employees or agents in the state, the Commissioner points to recent Supreme Court cases finding "minimum contacts", not dependent on in-state physical presence, to justify *in personam* jurisdiction of corporations.

In *Burger King Corp. v. Rudzewicz*, 471 U.S. 462 (1985) the plaintiff Florida corporation sued in the Florida Federal District Court a Michigan resident for breach of a franchise contract entered into in Florida, governed by Florida law and requiring payment of all fees and forwarding of all notices to plaintiff's headquarters in Florida. The defendant attacked the court's *in personam* jurisdiction. In affirming the lower court's finding of jurisdiction, the Supreme Court

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[2]"Benefits from the taxing State, unrelated to physical contact with the State, may be of vastly greater significance than those derived from the presence of a whole swarm of drummers soliciting business. Practically speaking, it is hardly essential to the existence of a nexus with the taxing State that there must be personnel, directly engaged in some form of physical activity within the State in furtherance of a business purpose. The *connection between the taxing State and the out-of-state collector-seller to establish nexus should be an economic rather than a physical relationship. When the out-of-state seller takes advantage of the economic milieu within the taxing State for the purpose of realizing a profit, a sufficient nexus to require the seller to collect the use tax could be found.*"

P. Hartman, *Federal Limitations on State and Local Taxation*, 631 (1981) (emphasis added). See also Hartman, 39 Vand. L. Rev. at 1014.

quoted from its opinion in *World-Wide Volkswagen Corp. v. Woodson,* 444 U.S. 286, 297-98 (1980) that "[t]he forum State does not exceed its powers under the Due Process Clause if it asserts personal jurisdiction over a corporation that delivers its products into the stream of commerce with the expectation that they will be purchased by consumers in the forum State." It enunciated the rule that "the constitutional touchstone remains whether the defendant purposefully established 'minimum contacts' in the forum State." Where the defendant "deliberately" engaged in "significant activities within a State" (*Keeton v. Hustler Magazine, Inc.,* 465 U.S. 770, 781 (1984)) or "has created 'continuing obligations' between himself and residents of the forum" (*Travellers Health Association v. Virginia* (339 U.S. 643, 648 (1950)); . . . [j]urisdiction in these circumstances may not be avoided merely because the defendant did not *physically* enter the forum State . . . So long as a commercial actor's efforts are 'purposely directed' toward residents of another State, we have consistently rejected the notion that an absence of physical contacts can defeat personal jurisdiction there." (471 U.S. at 476). See also *Asahi Metal Industry Co., Ltd. v. Superior Court of California,* 480 U.S. 102 (1987).

In *Keeton v. Hustler Magazine, Inc.,* 465 U.S. 770, 773-74 (1984) the Court held, "Respondent's regular circulation of magazines in the forum State is sufficient to support an assertion of jurisdiction in a libel action based on the contents of the magazines."

The Commissioner asserts that by Folio flooding Connecticut with its catalogs (649,000 in 1986, 733,000 in 1987) to solicit sale of its products, and by realizing sales revenues of over $2,000,000, its activities are "purposely directed" toward Connecticut residents, within the meaning of *Burger*

King Corp., and a nexus is established. He then invokes the leading case of *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977) which holds that a State tax on an out-of-state corporation does not violate the Commerce Clause when "[1] the tax is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State." Commissioner argues that if nexus with a state is adequate for due process purposes under the Fourteenth Amendment, it should be for taxing purposes under the Commerce Clause. See "Overturning Bellas Hess: Due Process Considerations." McCray, 1985 Brigham Young L. Rev. 265.

In this case the Connecticut use tax also meets the other prongs of the *Complete Auto* test. It is fairly apportioned because it provides a credit against it for sales taxes paid in other states (Conn. Gen. Stats. § 12-430(5)); it does not discriminate against interstate commerce because it is equal to the sales tax applicable to the same personal property purchased in-state. (*D. H. Holmes Company, Ltd. v. McNamara,* 406 U.S. 24 (1988)) and it is fairly related to services provided by Connecticut in that Connecticut provides the facilities and the "economic milieu" of a state that attracts Folio's upscale income customers, and the forum for enforcing Folio's legal rights against delinquent buyers. *Spiegel, Inc. v. FTC,* 540 F.2d 287 (7th Cir. 1976); see dissent in *National Bellas Hess,* 386 U.S. at 761-65; see also P. Hartman, infra, f. n. 1.

However, as persuasive as these arguments are, the Connecticut Supreme Court recently in *Cally Curtis Co. v. Groppo,* 214 Conn. 292 (1990) reaffirmed its allegiance to *National Bellas Hess. Cally Curtis* involved the issue of im-

posing a Connecticut use tax upon a California corporation which sold and rented training films to Connecticut residents, marketing them only by trade shows held outside of Connecticut and by sending catalogs through the mails. Orders for the film were accepted in California and deliveries and returns of films to and from Connecticut customers were made by common carrier or the United States mail. The Court held that "there was an insufficient nexus between *Curtis* and the state of Connecticut to subject *Curtis*, to the Connecticut use tax pursuant to General Statutes § 12-411." (214 Conn. at 301-2). The court found that *Curtis'* retention of title to the films it rented in Connecticut for three-day periods was de minimus and did not amount to holding property in the state. Relying strongly upon *National Bellas Hess*, it held that when a mail order corporation does not have property, agents, sales solicitors, retail stores, advertising offices, or local telephone listings, and does not advertise by radio, television, billboard or newspapers in a state, but communicates with customers in the state only by mail or common carrier, as part of a general interstate business, the corporation cannot constitutionally be required to collect that state's use tax.

This court finds the facts of *National Bellas Hess* and *Cally Curtis* indistinguishable from the facts of this case. Consequently, on the authority of those high court cases, this court is constrained to set aside the Commissioner's assessment of use taxes and license fees upon Folio. The appeal is sustained.

Robert Satter, J.

[Because of the length of the exhibits attached to this stipulation, none of the documents attached to this stipulation have been reproduced. The documents are on file in the clerk's office. (See P.B. sec. 4086)

NO. CV 87-0338611	
SFA FOLIO COLLECTIONS, INC.	SUPERIOR COURT
	JUDICIAL DISTRICT OF
v.	HARTFORD-NEW BRITAIN
	AT HARTFORD
TIMOTHY F. BANNON, COMMISSIONER OF DEPARTMENT OF REVENUE SERVICES OF THE STATE OF CONNECTICUT	February 2, 1989

STIPULATION OF FACTS

For purposes of the pending action only, it is stipulated by and between the parties, through their undersigned attorneys, that the following facts are admitted by the parties. No evidence of the facts set forth in this stipulation need be presented at trial. The parties further stipulate to the authenticity of the documents attached as exhibits hereto and made a part hereof and to the use of copies in lieu of originals for all purposes in this case.

The parties recognize that they have differing views as to the relevance of certain of the facts set forth below, even though the accuracy of those facts is not disputed. Accordingly, the parties specifically reserve the right to object to the relevance of any of the facts set forth in this stipulation.

I.

THE PARTIES

1. Plaintiff SFA Folio Collections, Inc. ("Folio") is a corporation organized and existing under the laws of the State of New York.

2. The officers and directors of Folio are located in New York City and Louisville, Kentucky.

3. Folio conducts a nationwide mail order business.

4. Folio is a wholly-owned subsidiary of Saks & Company ("Saks").

5. Folio's principal place of business is in Yonkers, New York.

6. Saks is a New York corporation with its corporate headquarters in New York City.

7. Defendant Timothy F. Bannon is the Commissioner of Revenue Services of the State of Connecticut ("the Commissioner"). He is responsible for the administration and enforcement of the Connecticut sales and use tax, Section 12-406 *et seq.* of Connecticut General States, Revision of 1949, as amended.

II.

FOLIO'S BUSINESS

8. Folio engages in mail order catalog sales from its principal place of business in Yonkers, New York. Written or telephone purchase orders from persons throughout the United States are received in Yonkers and merchandise is shipped therefrom by common carrier or U.S.

mail to fill these orders. Folio operates a tollfree "800" telephone number which its customers use to place their orders.

9. Folio has no retail stores anywhere.

10. Folio does not have, maintain, or physically use in Connecticut any store, office, distribution house, sales house, sample room, warehouse, other place of business, stock of goods, solicitor, canvasser, or sales person, at its direction, or with its permission. Folio has no written contract authorizing an agent or representative in Connecticut.

11. Folio neither owns nor leases real or personal property in Connecticut, but see paragraph 33.

12. Folio does not exhibit any goods or merchandise at leased space in Connecticut.

13. Folio stores no inventory or merchandise in Connecticut.

14. Folio has no offices in Connecticut.

15. Folio has no telephone service in Connecticut with local directory listings.

16. Folio is not qualified to do business in Connecticut.

17. Folio does not retain security interests in goods sold to Connecticut residents.

18. Folio does no credit investigations or collections in Connecticut.

19. Folio has no bank accounts in Connecticut.

20. Folio does not service or repair merchandise in Connecticut.

21. Folio sends mail order catalogs and flyers to Connecticut residents. In 1986, approximately 649,000 catalogs were sent to Connecticut residents. In 1987, approximately 733,000 catalogs were sent to Connecticut residents.

22. Folio has also contracted with companies such as Inserts, Inc., in Ridgefield, New Jersey, which places ads to sell catalogs several times a year in national fashion magazines such as Mademoiselle and Cosmopolitan. This company sells the mail order catalogs it advertises in these magazines.

23. Folio's catalogs are not designed, prepared, printed, published, or mailed from Connecticut.

24. Folio catalogs refer customers to its offices at 495 Tuckahoe Road, Yonkers, New York, for customer assistance, merchandise return or exchange, or other services. As a matter of policy, all customer service provided by Folio is provided at this location.

25. Customer inquiries and questions about orders are directed to Folio's offices in Yonkers, New York.

26. Customers pay for their orders by check or money order or by using their American Express, VISA, MasterCard, Saks Fifth Avenue, or Diners Club credit cards.

27. Folio's customers pay for shipping, handling, and transportation of mail order merchandise.

28. True and correct copies of Folio's catalogs are attached hereto as Exhibits 1-4 and are incorporated herein by reference.

29. "SFA" is an abbreviation for Saks Fifth Avenue. It is a federally registered tradename and trademark. It is part of Folio's corporate name and is used with the permission of Saks.

30. The name Saks Fifth Avenue has appeared in the Folio mail order catalog.

31. Saks Fifth Avenue and SFA are federally registered tradenames and trademarks. Their distinctive script designs are owned by the parent company, Saks & Company.

32. The Saks Fifth Avenue and SFA trademarks have traditionally signified high quality merchandise and service. To the extent that a Connecticut consumer associates these trademarks with Folio, Folio's business is benefitted.

33. Extra copies of certain Folio mail order catalogs are shipped by printers outside Connecticut via common carrier to the General Manager of the Saks Fifth Avenue store in Stamford for store employees to use as reference guides, to inform employees of fashion trends, and for merchandise education.

34. The credit department of Saks & Company includes advertising pieces, called "bill inserts," in the same envelope as charge account statements sent to customers. These bill inserts contain the toll-free number of Folio. To the extent any sales are generated from customers who receive bill inserts, the sales are filled by Folio. Folio pays the cost of the customer return envelope for the billing statement.

35. Tailoring services are available at the Saks Fifth Avenue-Stamford store. Folio customers who choose to

use the tailoring services are charged the standard fees by the store. These tailoring services are available at Saks Fifth Avenue stores to anyone as are other repair services, such as jewelry or watch repair.

36. All general merchants sell common goods at retail. A consumer may purchase the same brand name merchandise in a number and variety of different retail stores throughout the United States. The Saks Fifth Avenue store in Stamford sells some merchandise identical to that sold by Folio. Some merchandise in Folio's catalogs can be purchased from Connecticut retailers not affiliated in any way with Saks & Company.

37. Folio and Saks & Company share the following common director and officers:

Melvin Jacobs	– Chairman and Chief Executive Officer of Saks & Company Director of Folio
Joan F. Krey	– Vice President, General Counsel and Secretary of Saks Company Vice President and Assistant Secretary of Folio
Thomas F. D'Angelo	– Assistant Secretary of Saks & Company Vice President and Assistant Secretary of Folio

38. The attached Exhibit 5 lists common officers and directors of SFA Folio Collections, Inc. and Saks Fifth Avenue of Stamford, Inc. These officers and directors serve as representatives of the shareholders' interest, and are involved primarily in the financial oversight and gen-

eral protection of corporate interests. Responsibility for managing the day-to-day operations of both SFA Folio Collections, Inc., and Saks Fifth Avenue of Stamford, Inc., has been delegated to a separate management group in each corporation. None of the management group of SFA Folio Collections, Inc., makes any decisions for Saks Fifth Avenue of Stamford, Inc. None of the management group of Saks Fifth Avenue of Stamford, Inc., makes decisions for SFA Folio Collections, Inc.

39. All Saks Fifth Avenue retail stores and Folio share a great variety of daily sales data, monthly sales summaries, and sales and inventory levels by category and type of merchandise. They also share financial data and profit and loss statements.

40. From time to time, Folio may need to contact its Connecticut customers if their order forms are incomplete or incorrect. If additional information is needed to process a customer return or to make an adjustment, one of Folio's employees will call or write the customer.

41. A true and correct copy of the January 13, 1989 deposition of Joan F. Krey is attached hereto as Exhibit 6 and is incorporated herein by reference.

III.

CONNECTICUT USE TAX

42. Because it does not have employees, offices, or business locations in Connecticut, Folio never applied for and does not have a permit to collect use tax under Conn. Gen. Stat. § 12-409. It does not collect Connecticut use tax on its catalog sales to Connecticut residents.

43. On February 25, 1987, Joseph Thomas, a unit chief employed by the then Commissioner of Revenue Services John C. Groppo and acting under the direction and control of the Commissioner, informed Folio that it ". . . meets the definition of 'engaged in business in the state' as described in Section 12-407(15) of the Connecticut statutes. The unitary nexus established from your shared corporate name, logo, etc., with Saks Fifth Avenue-Stamford, Inc. is the basis of our position." Folio was asked to register with the Department and ". . . to charge appropriate sales tax . . ." on its sales to Connecticut residents.

44. Folio informed Commissioner Groppo that the imposition of a duty upon it to register under General Statute Section 12-411(8) was an invalid and unconstitutional application of Connecticut law and that he was without jurisdiction over Folio.

45. The Commissioner's reference to "Saks Fifth Avenue-Stamford, Inc." was to a separate Connecticut corporation. It is wholly-owned by Saks & Company. Saks Fifth Avenue-Stamford, Inc.'s only business is to run a retail store in Stamford, Connecticut.

46. On June 18, 1987, the Commissioner notified Folio that ". . . its registration application has been recently processed and the tax registration number . . ." 4920252-000 had been assigned to Folio. Folio never applied for a tax registration number.

47. On June 11, 1987, the Commissioner notified Folio that an assessment would be issued to it.

48. On July 1, 1987, the Commissioner sent a statement to Folio assessing sales and use tax liability in the

amount of $163,052.71, plus interest in the amount of $55,072.25 and a penalty of $16,305.32, for a total assessment at that time of $234,450.28.

49. On October 1, 1987, the Commissioner issued to Folio an assessment for a $20 sales and use tax license and permit.

IV.

ADMINISTRATIVE APPEAL

50. Pursuant to Connecticut General Statutes, Section 12-421, Folio filed its petition for reassessment with the Commissioner on July 30, 1987, citing to the Commissioner that it was not "engaged in business" in Connecticut as defined by Connecticut General Statutes, Section 12-407(15).

51. Folio also contended that it was not required to register with the Department of Revenue Services or to obtain a permit under Connecticut General Statute Ann., Section 12-409 because it was not engaged in or conducting business in Connecticut. Neither was Folio required to collect or liable for Connecticut sales and use taxes on its mail order sales to Connecticut customers.

52. Folio argued that the assessments purported to impose the duty of registration and of use tax collection upon it in violation of Connecticut law and United States constitutional provisions.

53. After consideration of Folio's appeal, the Commissioner denied it and confirmed the assessments on October 23, 1987.

54. Folio appealed to the Superior Court on November 20, 1987, pursuant to Connecticut General Statutes, Section 12-422.

55. The stipulated facts contained herein are to be used in the determination of Counts 1 and 3 of the complaint dated November 20, 1987, by the trial court. Pursuant to Practice Book § 4002, the parties consent that the determination of the issues involved in Counts 1 and 3 are of such significance to the determination of the outcome of the case, that the delay incident to appeal, with regard to Count 2 of the complaint, would be justified. The parties therefore consent to judgment being entered by the trial court on Counts 1 and 3 for the purpose of an immediate appeal pursuant to Practice Book § 4002 on those counts by the aggrieved party.

Count 2 of the complaint concerns the proper amount of tax and the proper amount of taxable sales. The parties stipulate that, if tax is due herein, this issue shall be remanded to the Department of Revenue Services for calculation of these amounts upon audit.

Respectfully submitted,

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5230T

BLOOMINGDALE'S BY MAIL, LTD.	IN THE CHANCERY COURT FOR
	THE STATE OF TENNESSEE
VS. NO 89-3017-II	
	TWENTIETH JUDICIAL DISTRICT
JOE B. HUDDLESTON, COMMISSIONER	DAVIDSON COUNTY, PART II

MEMORANDUM

This is an action for declaratory judgment and injunctive relief against the State's attempt to impose and enforce liability and use tax collection obligations on the plaintiff under the Tennessee statutes covering out-of-state mail-order companies.

Plaintiff claims it has no place of business, no property, and no employees in Tennessee, and therefore, no actual nexus or connection with the State. Plaintiff argues that the burden of collection unconstitutionally imposes a restraint upon interstate commerce and violates due process.

In particular, plaintiff relies on the decision in *National Bellas Hess, Inc. v. Illinois,* 386 U.S. 753, 87 S.Ct 1389, 18 L.Ed. 2d 505 (1967).

In determining whether a state tax complies with constitutional due process requirements, the controlling question is "whether the state has given anything for which it can ask return." *Bellas Hess,* 386 U.S. at 756. With regard to restraint on interstate commerce, the United States Supreme Court held that "state taxation falling on interstate commerce . . . can only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys." *id.* Accordingly,

when examining the constitutionality of imposing the duty of collection of the use tax upon an out-of-state seller, the relevant legal inquiry is whether there exists "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." The existence of such a link or nexus will thus turn upon the individual facts of each case. *L. L. Bean, Inc. v. Pennsylvania Department of Revenue,* 516 A. 2d 820 (1986).

Plaintiff has moved for summary judgment on the basis there are no issues of disputed fact. The summary judgment motion was heard on a stipulation and upon affidavits and depositions in support of and in opposition to the motion. Plaintiff has objected to affidavits filed by the defendant. The Court will first make a ruling on the objections.

The affidavit of Holly Ulrich, a professor of economics, as to changes in the mail order industry was objected to as irrelevant and hearsay. The affidavit presents the witness as a qualified expert in the field of economics. Attached to the affidavit is an unpublished paper entitled "Changes in the Mail Order Industry Since 1967." The affiant, as author of that paper, sets forth opinions and conclusions based on sources usually relied upon by expert in the field of economics.

This evidence is admissible under T.R.E. 702 and 703 and does have some relevance to this controversy.

The affidavit of Matthew N. Murray, a professor or economics, is objected to on the grounds of relevance and hearsay. Murray has also been qualified as an expert in economics and the evidence is also admissible under T.R.E. 702 and 703. The economic effect that plaintiff and other

mail order companies have on Tennessee has relevance to this case.

The affidavit of L. Eldridge concerning the weight of catalogs sent by plaintiff through the mail into Tennessee is objected to as irrelevant. This evidence is relevant to show that approximate amount of garbage the plaintiff regularly sends to Tennessee and the local government must dispose of.

The affidavit of Ray Westphal concerning modern computer use in computing taxes is objected to as irrelevant. One of the issues is the burden imposed on plaintiff in collecting taxes. The objection is overruled.

The part of the affidavit of Evelyn T. Gander that submits advertisements of Bloomingdale's, Inc., a separate corporation not a party in this case, is irrelevant and the objection is sustained.

The affidavit of May E. Bennett submitting defendants catalogs she received in Tennessee appears to have some relevancy and the objection is overruled.

Plaintiff objects to the affidavit of Charles L. Lewis as irrelevant. Plaintiff has admitted that it is within the precise scope of the mail order tax statute, T.C.A. § 67-6-102(6)(J), therefore, Mr. Lewis' affidavit is inadmissible.

Plaintiff also objects to portions of the deposition of Robert Vanmeter, plaintiff's chief financial officer, as set forth in the motion. The relevancy objections are overruled.

The State claims the mail order business today is vastly different from that in 1967, therefore providing nexus in this case that did not exist in *Bellas Hess*.

In the 1960's, the mail order business amounted to approximately $2.4 billion per year. By 1989 it increased to an estimated $183 billion.

Plaintiff solicits sales from Tennessee residents by the distribution of catalogs in a regular and systematic basis. Annually plaintiff distributes at least 25 different types of catalogs. From January to June of 1989, plaintiff distributed approximately 350,000 catalogs to Tennessee residents. The catalogs provide the customer a toll free number for placing orders or asking questions. Plaintiff accepts orders by mail order forms with payment by check, money order or credit card. Placing orders by telephone is the most frequently used method with payment by credit card.

At the time of the *Bellas Hess* decision, the necessity of a national company complying with combined local and state tax rates in several jurisdictions might have imposed a significant burden on interstate commerce. Those concerns have disappeared because of the capability of modern computers. In addition, Tennessee provides a dealer with the option of paying a uniform local rate. Therefore, the dealer selling to Tennessee residents need be concerned with only one tax rate for all of Tennessee.

The 350,000 catalogs shipped to Tennessee during six months from January to June of 1989 were printed on slick, non-recyclable paper. This requires local government to take on the burden of placing this garbage in landfills.

Plaintiff's sales catalog states that the merchandise ordered may be returned for replacement, credit or refund. This amounts to a "sale on approval" in which the goods remain the property of the seller until accepted by the buyer. Under this arrangement, title and risk of loss remains

with the plaintiff until acceptance. Thus, plaintiff has a considerable amount of property in Tennessee that requires local governments' protection from fire and theft.

If the *Bellas Hess* decision relied on the principle that exclusively interstate commerce is immune from state taxation, that principle was rejected in *Complete Auto Transit v. Brady,* 430 U.S. 274, 97 S.Ct. 1076, 51 L.Ed. 326 (1977).

In that case, the Supreme Court held that interstate commerce is required to pay its fair share of state taxes. The Court held a state sales tax on interstate commerce is valid if it satisfies a four prong test. The statutes in question satisfy that test.

It is not necessary to show the taxpayer has a "physical presence" in the taxing state in order to satisfy due process. In more recent years, the nexus test has been whether there is a minimal connection between the interstate activity and the taxing state. See *National Geographic v. California Equalization Board,* 430 U.S. 551, 97 S.Ct 1386, 51 L.Ed 631 (1977). The essence of the due process clause is to insure fundamental fairness.

In the case of out-of-state retailers enjoying large volumes of sales from the Tennessee marketplace, it is only fair and just for those retailers to collect taxes comparable to those collected by their local competitors.

The Court has, therefore, concluded that T.C.A. § 67-6-102(4)(J) and § 67-6-102(6)(J) area constitutional, and the State is entitled to a summary judgment.

General Lewis should prepare an order in accordance with this Memorandum.

C. ALLEN HIGH, CHANCELLOR

March 8, 1991
cc: Charles L. Lewis
Joe C. Peal
Maryann B. Gall
Joseph W. Gibbs

SFA FOLIO COLLECTIONS, INC.	IN THE CHANCERY COURT
VS. No. 89-3015-III	FOR THE STATE OF TENNESSEE
JOE B. HUDDLESTON, in his capacity as Commissioner of Revenue of the State of Tennessee	20TH JUDICIAL DISTRICT
	DAVIDSON COUNTY
	PART THREE

MEMORANDUM

This tax case is before the court on the plaintiff's motion for summary judgment. The principal question presented is whether the defendant Commissioner of Revenue's use tax assessment on the plaintiff's mail order sales to Tennessee residents violates the due process and commerce clauses of the United States Constitution. U.S. Const. art. 1, §8, cl. 3; amend. IV, §1.

The plaintiff SFA Folio Collections, Inc. is a New York State based mail order company that makes nationwide catalog sales, including sales to Tennessee residents. Orders and customer inquiries are directed to Folio's offices in

Yonkers, New York by mail and by a toll-free 800 telephone number. Merchandise is shipped directly to Tennessee customers from Yonkers, and all returns are directed there.

In June 1989, the Tennessee Department of Revenue notified Folio that it must register as a dealer for the purpose of collecting Tennessee use taxes under T.C.A. § 67-6-102(4)(J). A dealer includes any person who "[e]ngages in the regular or systematic solicitation of a consumer market in this state by the distribution of catalogs, periodicals, advertising fliers, or other advertising, or by means of print, radio or television media, by telegraphy, telephone, computer data base, cable, optic, microwave, or other communication system." In August 1989, the Department issued an assessment against Folio for the period January 1989 through June 1989.[1]

Folio argues in support of its motion that there are no contested facts and that T.C.A. § 67-6-102(6)(J) is unconstitutional, both facially and as applied to Folio. It contends that its only connection with Tennessee consists of communication with the state's residents via interstate commerce and therefore it lacks sufficient nexus with Tennessee to obligate it to collect state use tax.

Folio relies on the 1967 United States Supreme Court decision, *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753. In *Bellas Hess* the Court rejected an Illinois tax on mail order sales by an out-of-state company whose sole link with Illinois was through communication with residents by mail or common carrier. The Court held that in

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[1]The amount of the assessment was later reduced from $38,800 to $22,760.

light of due process of law and commerce clause requirements, such a link was not sufficient to justify state tax on the sales.

While the *Bellas Hess* case is instructive, it does not provide a complete answer to the present case. First, decisions in cases dealing with taxation on interstate commerce, including *Bellas Hess,* must be decided on their own peculiar facts. "Prohibited discriminatory burdens on interstate commerce are not to be determined by abstractions. Particular facts of specific cases determine whether a given tax prohibitively discriminates against interstate commerce." *Nelson v. Sears, Roebuck and Co.,* 312 U.S. 359, 366 (1941). This requires review of the totality of the out-of-state seller's activities within the taxing state. *See National Geographic society v. California board of Equalization,* 430 U.S. 551 (1977).

Second, the Court must consider the case in light of economic reality. *See Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 284 (1977). The technological and market-related changes since *Bellas Hess* cannot be ignored.

For Folio's commerce clause and due process of law claims, the controlling question is one of fairness – to the State as well as to Folio. While the commerce clause protects interstate commerce from unjustifiable local entanglements, a state may still require that interstate commerce bear a fair share of the cost of the local government whose protections it enjoys. *Bellas Hess,* 386 U.S. at 756. similarly, for due process of law, the issue is "whether the state has given anything for which it can ask return." *Id.* (citation omitted).

Folio repeatedly contacts Tennessee residents by mailing catalogs into Tennessee. The responsibility to dispose of

these catalogs falls upon Tennessee governments. Folio's frequent targeting of Tennessee residents must mean it has found Tennessee to be a fruitful marketplace. Fairness requires that it help pay for the cleanup in the aftermath of its frequent sales campaigns.

In Folio's marketing strategy customer satisfaction is central. Each catalog states in its order form:

"Satisfaction is guaranteed. If you are not satisfied, you may return your purchase for replacement credit or refund."[2] Until the buyer in Tennessee is satisfied with an order and the sale becomes final, Folio has an interest in goods that have come to rest in Tennessee. During that time, the laws of this state apply to these goods as to any other property within the state and protect Folio's interest. These laws permit a business like Folio to ship merchandise into Tennessee for customer inspection with the expectation that it will either profit from a sale or have its merchandise safely returned. Requiring Folio to bear some of the expense of this protection by collecting use tax is a fair demand.

No violation of the commerce clause results from imposing this duty. A major factor in the decision in *Bellas Hess* voiding collection of the Illinois use tax by an out-of-state mail order house was the unjustifiable entanglement of interstate commerce that would result if mail order businesses had to compute taxes from numerous local jurisdictions. 386 U.S. at 759-760. With the advantage in

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[2]Folio objects to the introduction into evidence of its own catalogs, asserting that they are "unauthenticated" and noting that they are not for the tax years in question. Significantly, Folio does not contend that the catalogs in the record are materially different from those from the tax years in dispute.

automation made since 1967, that holding in *Bellas Hess* is no longer valid. *See* Hartman, *Collection of the Use Tax on Out-of-State Mail-Order Sales,* 39 Vand. L. Rev. 993 (1986). Considering the technological support that Folio must use to operate an extensive and complicated mail order business, the collection of Tennessee use tax should not longer cause the problems feared in *Bellas Hess.*

The Court finds no violation of Folio's constitutional rights by the enforcement of T.C.A. § 67-6-102(6)(3). Folio's motion for summary judgment is denied.

ROBERT S. BRANDT
Chancellor

March 11, 1991
cc: Joseph Gibbs
Maryann B. Gall
Charles L. Lewis

IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
20TH JUDICIAL DISTRICT, DAVIDSON COUNTY,
PART THREE

SFA FOLIO COLLECTIONS, INC.	
VS.	
	No. 89-3015-III
JOE B. HUDDLESTON, in his capacity as Commissioner of Revenue of the State of Tennessee	

ORDER

For the reasons stated in the Court's Memorandum, the plaintiff's motion for summary judgment is denied.

ROBERT B. BRANDT
CHANCELLOR

March 11, 1991
cc: Joseph Gibbs
Maryann B. Gall
Charles L. Lewis

STATE OF NORTH DAKOTA
COUNTY OF BURLEIGH

IN DISTRICT COURT
SOUTH CENTRAL JUDICIAL DISTRICT

STATE OF NORTH DAKOTA, BY AND THROUGH ITS TAX COMMISSIONER, HEIDI HEITKAMP, Plaintiff,	CIVIL NO. 41677
- v. -	MEMORANDUM OPINION
QUILL CORPORATION, Defendant.	

This action brought by the State of North Dakota seeks to have the Quill Corporation declared a "retailer" for purposes of applying the North Dakota Sales and Use Tax on the distribution of Quill's products in our state. The Answer of Quill admits most of the facts alleged by the State, but specifically denies they are required to obtain a certificate of authority to do business in our state or that they are liable to remit a use tax on the products sold here. They specifically claim that the Tax Commissioner is acting in violation of the commerce clause of the United States Constitution.

The basis for taxation of products in North Dakota is Section 57-40.2-01(6) which amended the definition of "retailer" in 1987 to read as follows:

> "A retailer also includes every person who engages in regular or systematic solicitation of a consumer market in this state by the distribution of catalogs, periodicals, advertising fliers or other advertising, or by means of print, radio or television media, telegraphy, telephone, computer data base, cable, optic, microwave, or other communication system."

The facts of this matter show that Quill is a Delaware Corporation with its principal place of business in Illinois, with additional offices and warehouses in California. Quill solicits sales of merchanidse through catalogs and advertising flyers mailed to customers throughout North Dakota from locations outside of North Dakota. Quill does not maintain any office, distribution house, sales house, warehouse or any other place of business in North Dakota; it does not have any agent, salesmen, or other type of representative to sell or take orders, to deliver merchandise, to accept payments or to service merchandise it sells here; it does not have any telephone listing or toll free telephone line, and does not advertise by any radio or television media in North Dakota; It does not advertise in any newspapers distributed in North Dakota, nor solicit business in any fashion other than by catalog or flyer. All of the business conducted in North Dakota is done by United States mail, telephone or common carrier.

The point at which the parties depart in their interpretation of the facts is whether Quill has any real or personal tangible property in the State of North Dakota. The argument advanced by the state is that since Quill sells all of its items with an unequivocal ninety day guarantee, Quill remains the owner of such property until this approval period expires. Quill, on the other hand, claims that title passes at the time the property is shipped from their outlets in Illinois or California.

It seems clear to the Court that the case of *Hess v. Illinois*, 386 US 753 (1967) prohibits this type of legislation. In *Hess*, the facts are very similar to those found in this case. Hess was a mail order house with its principal place of business in Missouri. Its sales to Illinois residents were substantial.

Hess's manner of doing business in Illinois was similar to that of Quill in this case. The Supreme Court of the United States ultimately stated that there was insufficient nexus with the Hess Corporation to tax the sales that were taking place through the use of the mails.

In attempting to differentiate itself from that decision, the State, in this case, has chosen to identify the ninety-day guarantee as a "sale on approval". This argument has been advanced in numerous other states without success, and the Court finds no reason to adopt that theory here. I am satisfied that title changes hands at the time of the mailing, and that the risk on the items sold in this manner fall upon the purchaser in North Dakota at the time they receive the property, and not ninety days later as the state suggests.

Many of the arguments made by the State in this case are merely restatements of the remarks made by Mr. Justice Fortas in the *Hess* case. His dissent very logically sets forth reasons why *Hess* should have been taxed in Illinois, but the Supreme Court in that case failed to adopt his arguments. Although I find the arguments quite persuasive, this is not the law of the United States nor of the State of North Dakota.

Hess does, however, set forth the rationale for state taxation on interstate commerce. These concepts are set forth in the decision and read as follows:

> "State taxation falling on interstate commerce . . . can only be justified as designed to make such commerce bear a fair share of the cost of a local government whose protection it enjoys. . . . And in determining whether a state tax falls within the confines of the Due Process Clause, the Court has said that the simple but controlling question is whether the state has given anything for which it can ask return." See *Hess* at page 756.

Rather than dwell on the intricacies of title passing as the State has done in this case, they should have been presenting facts to the Court showing that the State of North Dakota spends funds for the protection and benefit of the mail order business. By doing so, they could show that taxation was not only for the benefit of local residents, but for the benefit of the mail order houses. Until these facts can be obtained, there is no nexus to allow the state to define retailer in the manner it chose. The mere fact that this appears to be unfair to the local retrailers cannot be a determining factor in this case. The focus must be on the beneficiary of the taxes as opposed to the consequences. Until this can be established, it would appear that the tax dollars spent protects the local resident and does not benefit the out of state mail order business in any significant manner.

The State, during argument, urged that the reasoning of *Goldberg v. Sweet,* 488 US ____ 102 LEd 2d 607, 109 S Ct 582 (1989), extends the taxing arm of the State to Quill. However, the primary difference in that case is that the parties stipulated Illinois had a substantial nexus with the interstate telecommunications reached by the Tax Act. That is precisely the issue in controversy in this case, and on which I fail to find any presence (nexus) of Quill in North Dakota.

Based on the foregoing, the language heretofore quoted in Section 57-40.2-01(6) and that found in subsection 7 is declared to be in violation of the United States Constitution and accordingly declared invalid as applied to Quill.

Counsel for the defendant may prepare the appropriate Order for Summary Judgment granting relief to them. The Court does not grant attorney's fees to the defendant, but only costs.

Dated: May 15, 1990

At Bismarck, North Dakota

BY THE COURT:

Benny A. Graff, District Judge

CONN. GEN. STAT. § 12-422

Appeal. Any taxpayer aggrieved because of any order, decision, determination or disallowance of the commissioner of revenue services under section 12-418, 12-421 or 12-425 may, within one month after service upon the taxpayer of notice of such order, decision, determination or disallowance, take an appeal therefrom to the superior court for the judicial district of Hartford-New Britain*, which shall be accompanied by a citation to the commissioner of revenue services to appear before said court. Such citation shall be signed by the same authority, and such appeal shall be returnable at the same time and served and returned in the same manner, as is required in case of a summons in a civil action. The authority issuing the citation shall take from the appellant a bond or recognizance to the state of Connecticut, with surety to prosecute the appeal to effect and to comply with the orders and decrees of the court in the premises. Such appeals shall be preferred cases, to be heard, unless cause appears to the contrary, at the first session, by the court or by a committee appointed by it. Said court may grant such relief as may be equitable and, if such tax has been paid prior to the granting of such relief, may order the treasurer to pay the amount of such relief, with interest at the rate of six per cent per annum, to the aggrieved taxpayer. If the appeal has been taken without probable cause, the court may tax double or triple costs, as the case demands; and, upon all such appeals which are denied, costs may be taxed against the appellant at the discretion of the court, but no costs shall be taxed against the state.

Supreme Court, U.S.
FILED
MAY 23 1991
OFFICE OF THE CLERK

No. 90-1627

IN THE
Supreme Court of the United States
OCTOBER TERM, 1990

COMMISSIONER OF REVENUE SERVICES
OF THE STATE OF CONNECTICUT,
Petitioner,
v.
SFA FOLIO COLLECTIONS, INC.,
Respondent.

On Petition for Writ of Certiorari to the Supreme Court of Connecticut

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Whether this Court should overrule its longstanding decision in *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), under which states can impose use tax collection obligations on out-of-state businesses only if they have a "physical presence" in the state.

2. Whether a state court decision interpreting state law to bar the attribution of activities of related corporations to the respondent (for purposes of determining its "physical presence" within the state) rests on an independent and adequate state ground.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

No. 90-1627

COMMISSIONER OF REVENUE SERVICES
OF THE STATE OF CONNECTICUT,
Petitioner,

v.

SFA FOLIO COLLECTIONS, INC.,
Respondent.

On Petition for Writ of Certiorari to the Supreme Court of Connecticut

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BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

STATEMENT

SFA Folio Collections, Inc. ("Folio") is a New York corporation that conducts a mail order business. Pet. App. A4, A30.[1] It is wholly-owned by Saks & Company ("Saks"), a New York corporation headquartered in New York City. *Id.* Folio solicits sales by sending catalogs to prospective customers, including customers in Connecticut. Pet. App. A5, A32. Customers place orders for merchandise displayed in the catalogs by contacting Folio directly in New York by mail or by using a toll free "800" number that puts them in contact with Folio employees in New York. Pet. App. A5-A6, A31-A32.

[1] Pursuant to Supreme Court Rule 29.1, the Court is advised that SFA Folio Collections, Inc. is a wholly-owned subsidiary of Saks and Company. SFA Folio Collections, Inc. has no subsidiaries.

Folio then ships the merchandise from New York to these purchasers by common carrier or United States mail. Pet. App. A6, A30-A31. Folio refers its customers to its New York facilities for customer assistance, merchandise return or exchange, and all other customer services. Pet. App. A6, A32.

Folio maintains no physical presence whatsoever in Connecticut; it conducts all of its business activities from its sole place of business in Yonkers, New York. Pet. App. A6, A31-A32. Folio does not operate retail stores anywhere, and does not maintain or use any store, office, warehouse, or other place of business in Connecticut. *Id.* Folio does not have any solicitors, agents, or representatives in Connecticut. *Id.* Folio has no inventory or merchandise in the state, and is not licensed to do business in Connecticut. *Id.* Folio has no telephone listing or bank accounts in Connecticut, does not retain security interests in any goods sold to Connecticut residents, and does not investigate credit or collect accounts in Connecticut. *Id.*[2] Folio does not design, prepare, print, publish or mail its catalogs in or from Connecticut. Pet. App. A5 n.3, A32. Folio's only contacts with Connecticut occur through the mail, common carriers, and "800" telephone lines. Pet. App. A6, A31-A32.

Folio's parent company, Saks, also owns Saks Fifth Avenue of Stamford, Inc. ("Saks-Stamford"), a Connecticut corporation that operates a retail store in Stamford, Connecticut. Pet. App. A5, A33-A34. Folio and Saks-Stamford are separate corporations. Pet. App. A5, A34-A35. The management decisions and day-to-day operations of each corporation are conducted by separate management groups that operate independently and autonomously; neither group makes decisions for the other corporation. Pet. App. A5, A35. To the extent that

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[2] Folio does not fill any order that is paid by check until after the check has been cleared by the bank, and, therefore, has no need to collect delinquent accounts in Connecticut. Pet. App. A5 n.4.

Folio utilizes advertising, marketing or merchandising services from its parent, Saks, it pays a fee for these services pursuant to a written agreement. Folio does not procure any of these services from Saks-Stamford.

Folio sells some of the same items that are available at Saks-Stamford, but many of these items are also available from retailers not affiliated in any way with Folio or Saks. Pet. App. A5, A34. Folio customers who choose to use Saks-Stamford's in-store tailoring services are charged the standard fees by the store; these services are available to anyone. Pet. App. A5, A33-A34.

Connecticut imposes a tax on the "acceptance, consumption or any other use . . . of tangible personal property purchased from any retailer" for use in the state. Conn. Gen. Stat. Ann. § 12-411(1) (West 1983 & Supp. 1990). The liability for the tax rests with the consumer (*id.* § 12-411(2)), but a "retailer" "engaged in business in the state" is obligated to collect the tax and remit it to Connecticut's taxing authorities (*id.* § 12-411(3)). The term "engaged in business in the state" was defined to require either the direct or indirect use "of any office, place of distribution, sales or sample room . . . or other place of business" in Connecticut, or the presence of a "representative, agent, salesman . . . or solicitor" in Connecticut. *Id.* § 12-407(15) (1987) (cited at Pet. App. A3).[3]

In February, 1987, the Commissioner of Revenue Services of the State of Connecticut (the "Commissioner") determined that Folio met the definition of "engaged in business in the state," and notified Folio that it must therefore register as a "retailer" and collect use tax on

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[3] This definition has since been broadened to encompass retail sales made from outside the state through "the distribution of catalogs, periodicals, advertising flyers or other advertising" in the state. Conn. Gen. Stat. Ann. § 12-407(15) (West Supp. 1990).

its Connecticut mail order sales. Pet. App. A36. Folio took the position that the attempt to impose these duties was an unconstitutional application of Connecticut law, and declined to register. *Id.* Therefore, to implement his decision, the Commissioner assigned Folio a tax registration number even though Folio had not applied for such a number. *Id.* On July 1, 1987, the Commissioner issued a $234,450.28 sales and use tax assessment against Folio for its failure to collect the tax. Pet. App. A4, A36-A37.

Folio petitioned for reassessment. Pet. App. A4. Folio asserted that it was not "engaged in business" in Connecticut for purposes of Conn. Gen. Stat. § 12-407(15), and thus not subject to tax. Pet. App. A4. Folio also argued that, in any event, it could not constitutionally be required to collect or pay Connecticut use tax. *Id.* The Commissioner denied Folio's petition. *Id.*

Folio appealed to the Connecticut Superior Court, which reversed. Pet. App. A21-A28. The court rejected the Commissioner's argument that the constitutional standards established in *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), were no longer applicable. Pet. App. A27-A28. Rather, applying *National Bellas Hess* to the facts at hand, the court concluded that "[t]he finding of the Commissioner's unit chief that Folio is engaged in business in Connecticut . . . has no basis in the evidence or in the law." Pet. App. A24.

The Commissioner appealed to the Connecticut Supreme Court, which unanimously affirmed. Pet. App. A1-A20. First, the Court rejected the Commissioner's argument that *National Bellas Hess* should be overruled. Pet. App. A16-A20. The Court concluded that the Commissioner's argument in large part tracked the arguments rejected in *National Bellas Hess* and "in essence parallel[ed] the reasoning of the dissent in *National Bellas Hess*." Pet. App. A20. Since the Commissioner's

position therefore had already been considered and rejected by this Court, the Connecticut Supreme Court declined to "dispense with the constitutional safeguards of the [commerce clause and the due process clause.]" Pet. App. A20.

Second, applying the standard established in *National Bellas Hess*, the court rejected the Commissioner's argument that Folio had sufficient nexus with Connecticut to "sustain the imposition of sales and use taxes." Pet. App. A7. This nexus, the Commissioner claimed, derived from Saks-Stamford, which operated a retail store in Connecticut. Although Saks-Stamford is a distinct corporation, the Commissioner argued that "their separate corporate existence should be disregarded and they should be treated as one enterprise for purposes of establishing a nexus for taxation." Pet. App. A11. After reviewing Connecticut corporate law and the Superior Court's factual findings, the court declined to "pierce the corporate veil" because the standard established by the Connecticut courts for doing so had not been met. Pet. App. A11-A12 (citing *Angelo Tomasso, Inc. v. Armor Construction & Paving, Inc.*, 187 Conn. 544, 557, 447 A.2d 406 (1982)). As the court explained, under Connecticut law, courts "pierce the corporate veil only under exceptional circumstances, for example, where the corporation is a mere shell, serving no legitimate purpose, and used primarily as an intermediary to perpetuate fraud or promote injustice." Pet. App. A11 (internal quotations and citations omitted). This petition followed.

REASONS FOR DENYING THE WRIT

I. THIS COURT SHOULD NOT GRANT CERTIORARI TO CONSIDER WHETHER TO OVERRULE *NATIONAL BELLAS HESS, INC. v. DEPARTMENT OF REVENUE.*

Petitioner candidly admits that the central focus of his petition is to "ask this Court to revisit its decision in *Bellas Hess.*" Pet. at 7. There is no reason to do so.

In *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), this Court held that states may not constitutionally require an out-of-state seller to collect use tax on mail order sales to residents of a state in which the seller's only contacts are by mail or common carrier. The Court found that such interstate communications did not create a "nexus" sufficient to support the imposition of use tax collection obligations without violating the Due Process Clause of the Fourteenth Amendment and the Commerce Clause. In reaching this result, this Court formulated the appropriate use tax nexus test by focusing on the seller's physical presence, *i.e.*, "retail outlets, solicitors, or property," "within the taxing state. *Bellas Hess*, 386 U.S. at 758. In *Bellas Hess*, the Court also refused to allow Illinois to impose use tax collection and payment obligations on the out-of-state mail order seller because it would create "unjustifiable local entanglements" of interstate commerce. *Bellas Hess*, 386 U.S. at 760. "The many variations in rates of tax, in allowable exemptions, and in administrative and recordkeeping requirements could entangle National [Bellas Hess'] interstate business in a virtual welter of complicated obligations to local jurisdictions . . . ." *Id.* at 759-60 (footnotes omitted).

The continuing validity of *National Bellas Hess* has been repeatedly recognized both by this Court [4] and the

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[4] *See infra* at 15.

lower state and federal courts, both for its central role in defining adequate nexus in state taxation cases,[5] and especially its control of use tax collection cases involving

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[5] *See, e.g., Alaska Airlines, Inc. v. Dept. of Revenue*, 769 P.2d 193, 198 (Or. 1989) (citing *Bellas Hess* "minimum connection" language as first prong of Commerce Clause test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), *infra* p. 15), *cert. denied*, 110 S.Ct. 717 (1990); *Good's Furniture House, Inc. v. Iowa State Bd. of Tax*, 382 N.W.2d 145, 150 (Iowa 1986) (State tax must meet nexus test articulated in *Miller Brothers Co. v. Maryland*, 347 U.S. 340 (1954), and refined by *National Bellas Hess* and *National Geographic Soc. v. California Bd. of Equalization*, 430 U.S. 551 (1977)), *cert. denied*, 479 U.S. 817 (1986); *Avco Financial Serv. Consumer Discount Co. One, Inc. v. Director Div. of Taxation*, 494 A.2d 788, 795 (N.J. 1985) (distinguishing *Bellas Hess* on ground of "distinctive contacts" with the State: "Unlike the mail order house in *National Bellas Hess*, or the department store in *Miller Brothers*," this seller "entered the taxing state to dun its customers," used "affiliated in-state offices for customers to drop payments," used the State's credit service agencies, and "invoked the State's process to enforce its contracts."); *National Meat Ass'n v. Deukmejian*, 743 F.2d 656, 658 n.1 (9th Cir. 1984) (comparing *National Geographic* and *Bellas Hess*, noting that factor establishing nexus in *National Geographic* was maintenance of offices in state), *aff'd*, 469 U.S. 1100 (1985); *Evanston Ins. Co., Inc. v. Merin*, 598 F. Supp. 1290, 1305 (D.N.J. 1984) (*Bellas Hess* is the "leading case defining the minimal connection required between an out-of-state business and a state before the state may impose tax liability," and "critical threshold" for triggering the power to tax is whether company "stations agents or establishes offices to conduct any business in the taxing state." *Id.* at 1306); *Illinois Com. Men's Ass'n v. State Bd. of Equal.*, 671 P.2d 349, 355 (Cal. 1983) (presence of agents in State formed "definite link" and "minimum connection" required to justify imposition of gross premium-tax), *appeal dismissed*, 466 U.S. 933 (1984); *Boswell v. Paramount Television Sales, Inc.*, 282 So.2d 892, 897 (Ala. 1973) (emphasizing that *Bellas Hess* requires physical presence); *Evansville-Vanderburgh Air. A.D. v. Delta Air., Inc.*, 265 N.E.2d 27, 28 (Ind. 1970) (citing *Bellas Hess* for "basic principle governing the power of a state to levy a tax affecting interstate commerce," "to make such commerce bear a fair share of the cost of the local government whose protection it enjoys").

out-of-state mail order houses.[6] The Connecticut Supreme Court was clearly correct in concluding that "[t]his appeal is governed by the United States Supreme Court decision in *National Bellas Hess, Inc. v. Department of Revenue*." Pet. App. A7.[7]

The sole conflicting appellate decision is a decision of the North Dakota Supreme Court rendered after the filing of the petition, in *North Dakota v. Quill Corp.*, No. 900257 (May 7, 1991).[8] The existence of that de-

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[6] *See, e.g., Cally Curtis Co. v. Groppo*, 572 A.2d 302 (Conn. 1990) (retention of title to films rented in State did not constitute sufficient nexus to support imposition of use tax collection obligations), *cert. denied*, 111 S.Ct. 77 (1990); *Bloomingdale's By Mail, Ltd. v. Commonwealth Dept. of Revenue*, 567 A.2d 773 (Pa. Commw. Ct. 1989) (invalidating collection obligations on out-of-state mail order house); *Burke & Sons Oil Co. v. Director of Revenue*, 757 S.W.2d 278, 280 (Mo.App. 1988) (citing *Bellas Hess* for proposition that "[m]erely communicating with customers in a state by mail or common carrier as part of a general interstate business does not create a sufficient nexus"); *L.L. Bean, Inc. v. Commonwealth of Pennsylvania*, 516 A.2d 820 (Pa. Commw. Ct. 1986) (invalidating collection obligations on out-of-state mail order house); *Aldens, Inc. v. Miller*, 466 F. Supp. 379, 383 (S.D.Iowa 1979) (state could not impose use tax collection obligations on out-of-state mail order insurance company) (dicta), *aff'd*, 610 F.2d 538 (8th Cir.), *cert. denied*, 446 U.S. 919 (1980); *Book-of-the-Month Club, Inc. v. Porterfield*, 268 N.E.2d 272, 274 (Ohio 1971) (invalidating imposition of use tax collection and payment obligations on out-of-state mail order book seller).

[7] The court reaffirmed the trial court's conclusion that the facts of *Bellas Hess* are "indistinguishable from the facts of this case." Pet. App. A8-A9.

[8] A copy of the *Quill* slip opinion has been lodged with the Clerk of this Court. While petitioner's position is also supported by a Tennessee trial court, *SFA Folio Collections, Inc. v. Huddleston*, No. 89-3015-III (Davidson Cty. Chancery Ct. Tenn. March 11, 1991) and *Bloomingdale's By Mail Ltd. v. Huddleston*, No. 89-3017-II (Davidson Cty. Chancery Ct. Tenn. March 8, 1991), the ruling in the *Blommingdale's* case is on appeal to the Tennessee Supreme Court and the *Folio* case has been placed on inactive status pending that appeal. Just last year, in *Pearle Health Services, Inc. v. Taylor*, 799

cision, which fails to give required deference to this Court's plain commands, does not suggest that certiorari should be granted.

In *Quill*, the court reviewed North Dakota's effort to impose use tax collection obligations on "every person who *engages in the regular solicitation* of sales of tangible personal property in this state by the distribution of catalogues, periodicals, advertising flyers or other advertising, by means of print, radio or television media, or *by mail* . . . ." (Emphasis supplied.)[9] Regulations pursuant to the statute defined "regular or systematic solicitation" as "three or more separate transmittances of any advertisement or advertisements" during the year. N.D. Admin Code § 81-04.1-01-03.1(3) (1984). The statute, in short, was designed to reach any mail order seller who made three or more solicitations by mail to residents of the state within a twelve-month period.

The district court invalidated the statute, noting that the State's arguments were "merely restatements" of the dissent in *National Bellas Hess*, which is "not the law of the United States nor of the State of North Dakota." *North Dakota v. Quill Corp.*, N. Dakota Tax Reports (CCH) ¶ 200-376 (May 15, 1990).

S.W.2d 655 (Tenn. 1990), the Tennessee Supreme Court recognized the continued viability of *Bellas Hess*. *Id.* at 658.

[9] Section 57-40.2-01(7), N.D. Cent. Code (Supp. 1989). The definition in its entirety is:

> "Retailer maintaining a place of business in this state", or any like term, shall mean any retailer having or maintaining within this state, directly or by a subsidiary, an office, distribution house, sales house, warehouse, or other place of business, or any agent operating within this state . . . . It also includes every person who engages in regular or systematic solicitation of sales of tangible personal property in this state by the distribution of catalogs, periodicals, advertising flyers, or other advertising, by means of print, radio or television media, or by mail, telegraphy, telephone, computer data base, cable, optic, microwave, or other communication system for the purpose of effecting retail sales of tangible personal property.

On review, the North Dakota Supreme Court acknowledged that in reaching this far, the statute was inconsistent with *National Bellas Hess*, which "drew a 'bright line' distinction between mail order sellers whose only connection with its customers in the taxing state was by common carrier or the United States mail and those with more significant connections with the state." *North Dakota v. Quill Corp.*, No. 900257, slip op. at 6 (N.D. Sup. Ct. May 7, 1991). Nonetheless, the court concluded "that the foundational basis of *Bellas Hess* has been eroded and that the Supreme Court would so conclude." *Quill*, slip op. at 12. In support of this remarkable conclusion, the North Dakota Supreme Court cited no decision of this Court questioning the continued validity of *National Bellas Hess*, nor even any dissenting opinion by any Justice that had done so since 1967. Rather, the state court quoted liberally from then-Justice Fortas' dissent in *National Bellas Hess* itself and concluded that the dissent accurately "forecast" the diminished value of that precedent. *Quill*, slip op. at 7.

The North Dakota Supreme Court has plainly failed to give appropriate deference to this Court's decisions. When a question of federal right is submitted to a state court, it is the duty of that court "to administer the law prescribed by the Constitution . . . as construed by this Court." *South Carolina v. Gailey*, 289 U.S. 412, 420 (1933).[10] This is so even in areas where, unlike the present situation, some doubt exists as to whether this Court would adopt the approach as an initial matter.

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[10] *See also, e.g., Cooper v. Aaron*, 358 U.S. 1, 18 (1958). ("The federal judiciary is supreme in the exposition of the law of the Constitution."); *Henry v. City of Rock Hill*, 376 U.S. 776, 777 n. (1964) (a Supreme Court decision interpreting the Federal Constitution, "under the Supremacy Clause, is binding upon state courts as well as upon federal courts"); *Chesapeake & Ohio Railway Co. v. Martin*, 283 U.S. 209, 221 (1931) (determination of a federal question by the Supreme Court "is binding upon the state courts and must be followed, any state law, decision, or rule to the contrary notwithstanding").

> If a precedent of this Court has direct application in a case, yet appears to rest on reasons rejected in some other line of decisions, the [lower courts] should follow the case which directly controls, leaving to this Court the prerogative of overruling its own decisions.

Rodriguez de Quijar v. Shearson/American Express, Inc., 490 U.S. 477, 484 (1989). "A different principle would lead to the most mischevious consequences. The courts of the several States might determine the same questions in different ways. There would be no uniformity of decisions."[11] This Court would be required to routinely exercise its certiorari jurisdiction to correct mere errors in the application of established precedent by the state courts.

Moreover, this Court has already considered, and rejected, the very arguments now advanced by the *Quill* court and by petitioner. In *Bellas Hess* itself the Court extensively discussed use tax nexus and rejected the dissent's contention that "systematic, continuous solicitation and exploitation" of a state's market should satisfy the constitutional requirement of nexus. *Bellas Hess*, 386 U.S. at 761 (Fortas, J., dissenting). Neither petitioner nor the *Quill* court has provided any grounds that would justify the Court's reconsideration of this same "economic presence" test, a concept directly and unequivocally repudiated in *Bellas Hess*.[12]

Aside from its reliance on the rejected "economic presence" argument and Justice Fortas' dissent in *National Bellas Hess*, the sole basis on which the North Dakota Supreme Court concluded that *National Bellas Hess* had

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[11] *The Mayor v. Cooper*, 73 U.S. (6 Wall.) 247, 253 (1867).

[12] The point had been forcefully argued in *Bellas Hess*. Appellee's Brief at 7-9, 18, *Bellas Hess* (O.T. 1966, No. 241) (state argued that sufficient nexus exists when seller, "in a systematic and continuous aggressive manner exploited the Illinois consumer market" by soliciting sales through catalog distribution).

been eroded was that the state court could not "ignore the tremendous social, economic, commercial, and legal innovations since 1967, and blindly apply an obsolescent precedent." *Quill*, slip op. at 9. The court first pointed to the increased volume of mail order business, finding that to be "the greatest change in mail order since 1967 . . . ." *Id.*, slip op. at 10. It also pointed to the new methods for ordering goods, including "toll-free telephone lines, fax orders, and direct computer ordering," and the new methods for delivery of such goods, including "advances in the parcel delivery industry . . . including overnight delivery . . . ." *Id.*, slip op. at 11. Neither the *Quill* opinion nor petitioner explains how any of this could have any relevance to the rationale of this Court's *National Bellas Hess* decision.

The actual volume of sales cannot alter the constitutional principles limiting a state's power to tax beyond its borders. In fact, the Court in *Bellas Hess* implicitly recognized that the constitutional rule announced in that case cannot fluctuate with quantitative factors such as sales volume or the size of the mail order industry. Although the Court was clearly aware that the sizable number of mail order sales at issue in 1967 [13] would increase in coming years,[14] the size of the industry itself did not affect the Court's constitutional analysis.

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[13] Bellas Hess' sales to Illinois residents in the fifteen month period at issue in that case totalled $2,174,744. *Bellas Hess*, 386 U.S. at 761 (Fortas, J., dissenting). Folio's sales to Connecticut residents in the *four year* period covered by the assessment were nearly identical: $2,174,036.30. *See* Pet. App. A22. Thus, Folio's annual sales were less than a third of National Bellas Hess' annual sales. Petitioner's emphasis on an "explosion" in the mail order industry overlooks the very substantial character of the mail order business directly at issue in *Bellas Hess*.

[14] It is evident from the dissent in *Bellas Hess* that the Court was cognizant of the substantial number of mail order sales and expected growth of the industry: "[T]his haven of immunity [for mail order sales] may well increase in size and importance." *Bellas Hess*, 386 U.S. at 764 (Fortas, J., dissenting).

Despite the assertions of the *Quill* opinion and petitioner (*Quill*, slip op. at 22, 26; Pet. at 10-11), there is also nothing "new" in the mail order industry that affects this Court's constitutional analysis of the burden imposed upon mail order houses for the collection of out-of-state use taxes. The burdensome compliance obligations that led the *Bellas Hess* Court to declare Illinois' assertion of tax jurisdiction unconstitutional have increased, rather than decreased, with the passage of time. The *Bellas Hess* Court noted that in 1965, "over 2,300 localities" imposed local sales tax (386 U.S. at 759 n.12); today, approximately 6,500 jurisdictions have the statutory authority to impose sales and use taxes. *See*, Note, *Collecting the Use Tax on Mail Order Sales*, 79 Geo. L.J. 535, 539 (1991). Today as in 1967, "[h]ardly two States provide identical exemptions," Appellant's Brief at 26-27, *Bellas Hess* (O.T. 1966, No. 241), but now, because of the growth in taxing jurisdictions, the exemption burden has grown almost threefold. Whereas 42 states had sales and use taxes in 1967, today 45 States and the District of Columbia have such taxes, adding even more burdensome recordkeeping requirements than drove the Supreme Court to invalidate the Illinois tax scheme in *Bellas Hess*.[15]

While computers might make it easier for mail order firms to calculate the tax due to each jurisdiction,[16] pro-

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[15] Aside from the enormous recordkeeping and record production requirements, the growth in the number of taxing jurisdictions raises the specter of nearly perpetual audits. *Interstate Sales Tax Collection Act of 1987: Hearing on H.R. 1242 Before the Subcomm. on Select Revenue Measures of the House Comm. on Ways and Means*, 100th Cong., 1st Sess. 31-32 (1987) (colloquy between Rep. Judd Gregg and Deputy Assistant Secretary of the Treasury O. Donaldson Chapoton). *Cf.* Appellant's Brief at 27-28, *Bellas Hess* (O.T. 1966, No. 241).

[16] However, Congressional testimony has strongly suggested that even this supposed benefit may be illusory. *See, e.g., Collection of State Sales and Use Taxes by Out-of-State Vendors: Hearing on*

found administrative burdens still remain, and collection obligations are still much more burdensome on mail order companies than on local retailers. Many customers still pay for mail order or merchandise by check and money order, and often make mistakes in calculating tax.[17] The mail order house must either pay the tax itself or bill the customer for the additional tax.[18] Computerization at the mail order house does little to solve these problems. "On average, mail-order companies bear six or seven times the collection costs of in-state retailers who can collect sales tax at the cash register." Note, 79 Geo. L.J. at 541. Far from receding with the passage of time, the compliance burdens on out-of-state mail order companies have actually grown.

In addition to relying on supposed changes in the mail order industry, the *Quill* opinion and the petitioner here, Pet. at 12-13, claim that this Court's decisions have undermined *National Bellas Hess*. The *Quill* opinion urged that "the most striking shift in the Court's position on taxation of interstate commerce occurred in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977)," in which this Court announced a four-part test for invali-

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S. 639 and S. 1099 Before the Subcomm. on Taxation and Debt Management of the Senate Comm. on Finance, 100th Cong., 1st Sess. 52 (1987) ["*Hearing on S. 639 and S. 1099*"] (testimony of Alan Glazer). Witnesses have also noted that computer tax programs are not equipped to recognize tax exemptions for products, which vary from jurisdiction to jurisdiction, nor can such programs judge whether products fit within a given exemption. *See, e.g., Interstate Sales Tax Collection Act of 1987: Hearing on H.R. 1242 Before the Subcomm. on Select Revenue Measures of the House Comm. on Ways and Means*, 100th Cong., 1st Sess. 178 (1987) (testimony of Heath Kline); *Hearing on S. 639 and S. 1099* at 53 (testimony of Robert Levering).

[17] Even the computer tax programming industry itself admits that this burden cannot be lifted by computer technology. *Hearing on S. 639 and S. 1099* at 206 (letter from Ray Westphal, President, Vertex Systems).

[18] Conn. Gen. Stat. § 12-411(3).

dating state taxation under the Commerce Clause. *Quill*, slip op. at 12.[19] However, *Complete Auto Transit* continued to require a showing of "substantial nexus," and this Court on at least two occasions since the decision in *Complete Auto Transit* has reaffirmed *National Bellas Hess*, and made clear that the decision was entirely consistent with the *Complete Auto Transit* decision.

In *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981), the Court noted that *National Bellas Hess* is the touchstone of the first prong of *Complete Auto Transit*: "Under this threshold test, the interstate business must have a substantial nexus with the State before *any* tax may be levied on it. See *National Bellas Hess, Inc. v. Illinois Revenue Dept.*, 386 U.S. 753 (1967)." *Commonwealth Edison*, 453 U.S. at 626. (emphasis in original). And as recently as 1988, this Court unanimously reaffirmed its *Bellas Hess* holding in *D.H. Holmes Co. v. McNamara*, 486 U.S. 24, 33 (1988):

> In *National Bellas Hess*, we held that the State of Illinois could not, consistently with the Commerce Clause, compel an out-of-state mail order company to collect a use tax on purchases of goods by Illinois residents when the seller's only connection with its Illinois customers was by mail or common carrier.

See also National Geographic Society v. California Board of Equalization, 430 U.S. 551 (1977).

Neither the *Quill* opinion nor petitioner cites a single decision of this Court that questions the continued validity of *Bellas Hess*.[20] Instead they rely on personal juris-

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[19] Under that test, a state tax will be sustained so long as "the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State." 430 U.S. at 279.

[20] This Court in *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 483 U.S. 232 (1987)—a decision relied on

diction cases (*see Quill*, slip op. at 18-21; Pet. at 8-9) that exclusively address the due process concerns that limit a state's exercise of *personal* jurisdiction over a nonresident.

Again the *Quill* opinion and petitioner fail to note that the Court in *Bellas Hess* refused to adopt a standard fashioned from these personal jurisdiction nexus cases. In *Bellas Hess*, the state directly urged the Court to adopt the economic presence test that had already been applied in personal jurisdiction cases for at least ten years. *See* Appellee's Brief at 32-34, *Bellas Hess* (O.T. 1966, No. 241). This Court declined to adopt the personal jurisdiction test in the tax area, and held in *Bellas Hess* that even continuous and systematic solicitation by mail cannot create tax nexus when the taxpayer is not physically present in the state.

In short, while the decision of the North Dakota Supreme Court may provide an adequate ground for summary reversal in that case, as authorized by Rule 16.1 of the Rules of this Court,[21] it provides no ground for granting certiorari in this case.

Clearly, petitioner addresses his argument to the wrong forum when he expresses continued dissatisfaction with the impact of *National Bellas Hess* upon his ability to collect use taxes on goods purchased by Connecticut consumers. Congress has authority to fashion an equi-

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in the *Quill* opinion (slip op. at 18) and by petitioner (Pet. at 8-9) —did not do so directly or by implication. It upheld taxing jurisdiction because the taxpayer's employee resided in the state and performed substantial activities on the taxpayer's behalf there. Thus, the taxpayer maintained a significant physical presence in the state. In *Standard Pressed Steel v. Washington Department of Revenue*, 419 U.S. 560 (1975), also relied on in *Quill* (slip op. at 16-18), this Court similarly upheld imposition of the state's business and occupation tax on a company because its employee had "a full-time job within the State . . . ." *Id.* at 562.

[21] *See* R. Stern, E. Gressman, and S. Shapiro, *Supreme Court Practice* § 5.19 at 296-97 (6th ed. 1986).

table and forward-looking system for the collection of state use taxes by out-of-state sellers that will avoid upsetting the settled expectations of the parties and the burdens and inequities that individual state and local collection efforts would impose. Congress is well aware of the claims of the state taxing authorities: in recent years numerous bills have been introduced to achieve legislatively the goal that petitioner seeks here.[22] While there is debate about the form that such legislation should take, some of these proposals would seek to address the substantial compliance burdens for out-of-state mail order firms and their customers by establishing a uniform national rate of tax, an adequate collection allowance, a uniform definition of exempt items, a uniform tax treatment of shipping and handling charges, and a single filing and audit procedure.[23]

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[22] *See, e.g.*, S. 2368, 100th Cong., 2d Sess. (1988); H.R. 3521, 100th Cong., 1st Sess. (1987); H.R. 1891, 100th Cong., 1st Sess. (1987). Hearings have been conducted on many of these pending bills, as well as former legislative proposals. *See, e.g., State Taxation of Interstate Commerce: Hearing on S. 1510 Before the Subcomm. on Taxation and Debt Management of the Senate Comm. on Finance*, 99th Cong., 1st Sess. (1985); *Interstate Sales Tax Collection Act of 1987: Hearing on H.R. 1242 Before the Subcomm. on Select Revenue Measures of the House Comm. on Ways and Means*, 100th Cong., 1st Sess. (1987); *Collection of State Sales and Use Taxes by Out-of-State Vendors: Hearing on S. 639 and S. 1099 Before the Subcomm. on Taxation and Debt Management of the Senate Comm. on Finance*, 100th Cong., 1st Sess. (1987); *Interstate Sales Tax Collection Act of 1987 and the Equity in Interstate Competition Act of 1987: Hearings on H.R. 1242, H.R. 1891, and H.R. 3521 Before the Subcomm. on Monopolies and Commercial Law of the House Comm. on the Judiciary*, 100th Cong., 2d Sess. (1988).

[23] *See, e.g.*, Committee on State Taxation of the Counsel of State Chambers of Commerce, *COST Endorses Compromise on Bellas Hess Legislation*, State Tax Report No. 244 at 1 (Dec. 15, 1989).

II. IN DECLINING TO ATTRIBUTE THE ACTIONS OF RELATED CORPORATIONS TO FOLIO, THE CONNECTICUT SUPREME COURT'S DECISION WAS BASED UPON AN ADEQUATE AND INDEPENDENT STATE GROUND.

Although petitioner primarily contends that this Court should "revisit" its decision in *Bellas Hess*, petitioner also intimates that an alternate ground exists for review in this case. *See* Pet. at 10-11. Petitioner suggests that Folio has sufficient nexus with Connecticut, even under the *Bellas Hess* rule of physical presence, because Folio is part of a larger enterprise of affiliated corporations and should be deemed to share the nexus that Saks-Stamford has with Connecticut. *See* Pet. at 7. The Connecticut Supreme Court treated this issue purely as a question of state corporate law.[24] As a result, its decision on this point rests on adequate and independent state grounds and is not subject to further review by this Court. *See generally* R. Stern, *supra* note 21, § 3.25 at 168.

The state court's opinion relied solely on principles of Connecticut corporate law in rejecting an "enterprise" theory and refusing to impute Saks-Stamford's activities to Folio. The Connecticut Supreme Court characterized the "enterprise" issue as one of state law by first referring to the traditional corporate theories of "piercing the corporate veil" and "alter ego," and then summarizing the Commissioner's position as one seeking to "disregard" the separate corporate existence of Folio and Saks-Stamford. Pet. App. A10, A11. Equally clear is the court's extensive consideration and application of these corporate law principles in reaching its result:

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[24] In addition, the Connecticut Supreme Court affirmed the Superior Court's factual finding that "Saks-Stamford is not Folio's retail store, agent, instrumentality, or alter ego." Pet. App. A24.

> It is undisputed that in Connecticut a court will disregard the corporate structure and pierce the corporate veil 'only under exceptional circumstances,' . . . . Nevertheless, the commissioner seeks to have this court abandon our traditional notions of corporate law and ignore Folio's separate corporate existence under an enterprise theory.

Pet. App. A11-A12. In refusing to "abandon [Connecticut's] traditional notions of corporate law," the court noted that:

> Clearly, there is no statute within the Connecticut sales and use tax chapter . . . that allows the commissioner to treat separate corporations as part of one enterprise for the purpose of imposing sales and use tax liability, and the commissioner does not make such a claim. Absent such statutory authority, the line of cases pursuant to the 'unitary business principle' are inapplicable.

Pet. App. A12-A13. Relying on the "fundamental principle of corporate law that 'the parent corporation and its subsidiary are treated as separate and distinct legal persons,' " the court concluded that "we would not be justified in disregarding Folio's separate identity for tax purposes." Pet. App. A13, A15.

The decision shows that the Connecticut Supreme Court relied exclusively on state corporate law principles to find that the in-state presence of Saks-Stamford was irrelevant to Folio's tax liability in Connecticut. Inasmuch as the Connecticut Supreme Court disposed of the enterprise theory solely on state law grounds, petitioner cannot now resurrect this theory as an alternate ground for review. *See, e.g., Klinger v. Missouri*, 80 U.S. (13 Wall.) 257, 263 (1871); *see also Michigan v. Long*, 463 U.S. 1032, 1037-39 (1983); *Ridgway v. Ridgway*, 454 U.S. 46, 54 (1981); *Zacchini v. Scripps-Howard Broadcasting Co.*, 433 U.S. 562, 566 (1977).

CONCLUSION

The petition for a writ of certiorari should be denied.

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BRIEF OF THE STATE OF CALIFORNIA AS AMICUS CURIAE IN SUPPORT OF PETITIONER

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INTEREST OF THE AMICUS CURIAE, STATE OF CALIFORNIA

The State of California, on behalf of the California State Board of Equalization, submits this brief as amicus curiae in support of petitioner, Commissioner of Revenue Services of the State of Connecticut. Since this brief is being filed by the State of California and is sponsored by the California Attorney General, consent to its filing is not required. United States Supreme Court Rule 37.5.

At issue in this case is whether Connecticut can, consistent with the Due Process and Commerce Clauses, require out-of-state mail order companies to collect use taxes from that state's customers in situations where the companies conduct substantial and recurring solicitations and sales in the state.

In addition to the state court actions referenced by petitioner,[1] California is presently involved in four separate actions, two in federal district court,[2] two in California state courts,[3] each of which involve this same issue

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[1] Petition at pages 7 and 12.

[2] *Direct Marketing Association v. William M. Bennett, et al.*, CV-S-88-1067-MLS, (E.D. Cal.); *Olde Salmon Falls Corp. v. William M. Bennett, et al.*, CIVS-91-306 EJG-JFM (E.D. Cal.). In the former case, the district court ruled that plaintiff trade association has standing so that the application of plaintiff to enjoin California from enforcing its use tax enforcement statute, section 6203(f), California Revenue & Taxation Code, is proceeding to judgment. The latter case, recently filed, seeks a judicial determination that, based upon this same statute, California cannot constitutionally require plaintiff to collect and remit California use taxes. Section 6203(f) contains explicit guidelines for the enforcement of use tax collection duties of out-of-state mail order sellers.

[3] *Lands' End, Inc. v. California State Board of Equalization*, No. 620135, Superior Court of California, San Diego County (appeal pending); *Sturbridge Yankee Workshop, Inc. v. State Board of Equalization*, No. 512584, Superior Court of California, Sacramento County (California expects that the notice of appeal in this matter will be filed within a matter of days). In both cases, the trial courts ruled that each plaintiff has insufficient "nexus" with California to constitutionally permit assertion of the state's use tax collection requirement predicated on section 6203(f), California Revenue & Taxation Code.

and are presently in varying procedural postures.[4]

This case presents the Court with the opportunity to address the significant technological changes utilized by mail order companies since this Court's decision in *National Bellas Hess v. Department of Revenue,* 386 U.S. 753 (1967), to consider the "economic realities" of the substantial exploitation of local markets by such entities, and to provide guidance in resolving the numerous pending federal and state cases by announcing the legal standard applicable to the efforts (including legislative enactments) of many states to require such entities to collect and remit use taxes.

SUMMARY OF ARGUMENT

The mail order industry no longer involves twice-a-year catalogs supplemented by occasional mailings and customer contacts limited to common carriers and the postal service, while as many as 2,300 jurisdictions, with varying rates, attempt to assess use taxes (*National Bellas Hess, supra,* at 754-55, 759). Mail order retailers now exploit local markets through the use of "800" telephone numbers (some available 24 hours every day), through voluminous catalog mailings and through the acceptance

[4] Additionally, the *Direct Marketing Association v. William M. Bennett, et al.* matter has this term been the subject of a certiorari petition by California (Case No. 90-1400) which sought this Court's review of the Ninth Circuit's application of the Tax Injunction Act (28 U.S.C. § 1341) to California's use tax claim and refund statutes. This Court denied the petition.

of credit cards for purchases. Those credit card systems permit the mail order company to be electronically and almost instantaneously advised whether the financial institution which issued the card approves the purchase and thus, in effect, guarantees payment to the seller. At the same time, states such as California have limited the mail order companies' use tax collection requirement to a single uniform statewide rate,[5] so that the impediments to interstate commerce envisioned by this Court in *National Bellas Hess* (*supra*, at 759) are no longer a reality. The rationale no longer exists to permit mail order companies to ignore a state's use tax collection requirements at the same time substantial sales are made in the same state.

ARGUMENT

I. THE VOLUME AND METHODS OF MAIL ORDER BUSINESS FAR EXCEED THAT BEFORE THE COURT IN *NATIONAL BELLAS HESS.*

The mail order company in *National Bellas Hess* utilized twice-a-year catalog mailings supplemented by occasional advertising "flyers" and mail and/or common carrier customer contacts, which resulted in an unspecified amount of sales in that state. (*Id.*, at 754-55.)[6] Cali-

[5] Section 6203(j), California Revenue & Taxation Code.

[6] The dissenting opinion referenced sales figures but the same were not mentioned by this Court in its decision.

fornia agrees with Connecticut[7] that now the methods utilized by mail order companies to conduct local business are far different and permit substantial sales in a single state.

For example, in the *Lands' End* matter (fn. 3, *supra*), the parties stipulated that: 1) in (fiscal) 1989, Lands' End had 13 catalog issues with an average of 156 pages per issue involving the mailing of approximately 75 million catalogs; 2) in calendar 1989, Lands' End's California sales exceeded $63,000,000 with total sales in excess of $543,000,000; 3) that for 90 to 95 percent of the shipments of goods to California customers, two to three times a week truck trailers owned by another company are loaded with packages at Lands' End's distribution center and the trailers deliver these packages to a United Parcel Service facility in Los Angeles for ultimate delivery to customers; 4) that 600 "800" telephone lines (involving no cost to customers for any calls) for customer orders are available 24 hours every day except Christmas; and 5) that 86 per cent of Lands' End's sales are made through acceptance of a customer's credit card, with a substantial portion of such sales to California customers effectuated through acceptance of credit cards issued by California financial institutions.[8]

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[7] Petition, at 10–13.

[8] While the particulars of the business practices of other mail order companies may not exactly parallel those of Lands' End, California understands that significant and continuing catalog solicitations, "800" lines, and a high percentage of sales by credit card are the norm for mail order companies.

The acceptance of credit cards is among the most important methods through which mail order companies now conduct business.

In *Colorado Springs National Bank v. United States,* 505 F.2d 1185 (10th Cir. 1974), the Court of Appeals engaged in an extended discussion of the mechanics of credit card transactions.[9] As that court noted, utilizing even the technology and computers available by 1974, the merchant, by honoring the credit card, is paid, at a discount, by the bank which issued the card, with the card user liable to the issuing bank. (*Id.,* at 1190.)

California has learned, through discovery in cases including *Lands' End, supra,* that mail order retailers are provided by their own credit card merchant banks[10] with electronic equipment permitting retailers to be electronically and almost instantaneously advised whether the bank which issued the credit card will approve the purchase. Mail order merchants who obtain such electronic purchase authorizations record that the approval was obtained, provide the merchant banks with the approval information, and thus insure that payment, at a discount, will be forthcoming, with the card-issuing bank liable for collecting the debt from the card holder. In fact, since validly obtaining approval authorization insures payment

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[9] The legal issue addressed was the deductibility of expenses associated with credit card start-up costs.

[10] These are the banks to which mail order companies submit approved credit card charges for payment, so that the transactions are processed through the credit card systems and ultimately billed to the customer's account.

to the seller for credit card sales, the practice of the industry is to decline credit card sales where the issuing bank, or an entity authorized to act on behalf of the bank, has not given the electronic approval.

II. THE RATIONALE NO LONGER EXISTS FOR EXEMPTING MAIL ORDER COMPANIES FROM COLLECTING STATE USE TAXES ABSENT SUCH COMPANIES HAVING PHYSICAL PRESENCE IN THE TAXING STATE.

The potential "welter of complicated obligations to local jurisdictions with no legitimate claim" to make mail order retailers collect use taxes (*National Bellas Hess, supra,* at 760), previously relied upon by this Court to strike down Illinois' effort to require a mail order company to collect that state's use taxes, is no longer a problem, particularly as to California and other states which limit use tax collection requirements to a single statewide rate. (See California Revenue & Taxation Code, section 6203(j).) Claims of undue burden, even assuming *arguendo* that a number of jurisdictions in any other state could assert a use tax collection obligation as to any particular mail order retailer, appear frivolous in the face of the reliance of modern business on computers and similar equipment. This is especially true considering the utilization by mail order companies of the national credit card systems involving the electronic authorization process which is employed for every single credit card transaction.

To the extent the "physical presence" standard for permitting a state to assert a use tax collection requirement (*National Bellas Hess, supra,* at 758) retains any validity, it is important to note that this Court's reference to "retail

outlets, solicitors, or property within a state" was contrasted with companies which "do no more than communicate with customers in the State by mail or common carrier." However, mail order companies now participate, without the involvement of mail or common carriers, in national credit card systems, which can (and do) involve substantial connections with the state asserting a use tax collection duty. For example, to the extent that the banks which issue the credit cards maintain such accounts and provide approval authorization, are situated and perform such functions in the same state where the customer lives, these activities involve substantial business being conducted in that state, business in which the mail order companies participate. In the circumstances involving such credit card transactions, certainly the activities in the state asserting the use tax collection requirement far exceeds that of the 10 solicitors who worked in Florida and whose activities were found sufficient to require use tax collection by this Court in *Scripto, Inc. v. Carson,* 362 U.S. 207, 211-12 (1960).

CONCLUSION

For the reasons stated, this Court should address the constitutionality of the states' use tax collection requirements in the context of how the mail order companies now conduct business (including utilization of the credit card systems) and how such business permits substantial exploitation of local markets making collection of use taxes absent any constitutionally infirm burden.

Respectfully submitted,

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California Revenue & Taxation Code, Section 6203

§ 6203. Collection of tax by retailer; Receipt to purchaser; "Retailer engaged in business in this State"

Except as provided by Sections 6292 and 6293, every retailer engaged in business in this state and making sales of tangible personal property for storage, use, or other consumption in this state, not exempted under Chapter 3.5 (commencing with Section 6271) or Chapter 4 (commencing with Section 6351), shall at the time of making the sales or, if the storage, use, or other consumption of the tangible personal property is not then taxable hereunder, at the time the storage, use, or other consumption becomes taxable, collect the tax from the purchaser and give to the purchaser a receipt for the tax in the manner and form prescribed by the board.

As respects leases constituting sales of tangible personal property, the tax shall be collected from the lessee at the time accounts are paid by the lessee under the lease.

"Retailer engaged in business in this state," as used in this section and in Section 6202, means and includes any of the following:

(a) Any retailer maintaining, occupying, or using, permanently or temporarily, directly or indirectly, or through a subsidiary, or agent, by whatever name called, an office, place of distribution, sales or sample room or place, warehouse or storage place, or other place of business.

(b) Any retailer having any representative, agent, salesperson, canvasser, or solicitor operating in this state under the authority of the retailer or its subsidiary for the

purpose of selling, delivering, or the taking of orders for any tangible personal property.

(c) As respects a lease, any retailer deriving rentals from a lease of tangible personal property situated in this state.

(d) Any retailer soliciting orders for tangible personal property by means of a telecommunication or television shopping system (which utilizes toll free numbers) which is intended by the retailer to be broadcast by cable television or other means of broadcasting, to consumers located in this state.

(e) Any retailer who, pursuant to a contract with a broadcaster or publisher located in this state, solicits orders for tangible personal property by means of advertising which is disseminated primarily to consumers located in this state and only secondarily to bordering jurisdictions.

(f) Any retailer soliciting orders for tangible personal property by mail if the solicitations are substantial and recurring and if the retailer benefits from any banking, financing, debt collection, telecommunication, or marketing activities occurring in this state or benefits from the location in this state of authorized installation, servicing, or repair facilities.

(g) Any retailer owned or controlled by the same interests which own or control any retailer engaged in businesses in the same or similar line of business in this state.

(h) Any retailer having a franchisee or licensee operating under its trade name if the franchisee or licensee is required to collect the tax under this section.

(i) Any retailer who, pursuant to a contract with a cable television operator located in this state, solicits orders for tangible personal property by means of advertising which is transmitted or distributed over a cable television system in this state.

(j) Notwithstanding Section 7262, a retailer specified in subdivision (d), (e), (f), (g), (h), or (i) above, and not specified in subdivision (a), (b), or (c) above, is a "retailer engaged in business in this State" for the purposes of this part and Part 1.5 (commencing with section 7200) only.

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SUPPLEMENTAL BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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ARGUMENT

Pursuant to Supreme Court Rule 15.7, petitioner submits this supplemental brief calling the Court's attention to a recent decision of the Supreme Court of North Dakota that is in direct conflict with the decision of the Connecticut Supreme Court in this case.

In *North Dakota v. Quill,* No. 900257 (N.D. May 7, 1991) (App. p. A1), the Supreme Court of North Dakota unequivocally rejected as outdated this Court's holding in *National Bellas Hess v. Department of Revenue,* 386 U.S. 753 (1967), that a mail order seller without a physical presence in a state cannot constitutionally be required to collect the state's sales and use tax. The North Dakota decision conflicts with the decision of Connecticut's Court to follow *Bellas Hess* and preclude application of Connecticut's sales and use tax to such mail order companies. The Court should grant the petition to resolve this conflict and to address the recurrent issue of the constitutionality of states' application of their sales and use tax to mail order sales.[1]

Under the Connecticut sales and use tax, all retailers making sales in Connecticut are required to collect use tax from their customers. Conn. Gen. Stat. § 12-411(3). The issue presented is whether a mail order company's systematic and continuous solicitation of orders by mailing hundreds of thousands of unsolicited catalogs to Connecticut customers constitutes sufficient nexus with

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[1] Connecticut recognizes that the Court may choose to hold the petition in this case until a petition for certiorari may be filed in *North Dakota v. Quill,* and set the cases for argument in tandem if the petitions are granted. Connecticut believes,

(Continued on following page)

the state to require, consistent with the Due Process and Commerce Clauses, collection of the sales and use tax. Specifically, the question at issue is whether this Court's holding in *Bellas Hess,* decided a quarter of a century ago, remains a valid interpretation of the constitutional limitations on a state's right to tax.

The Connecticut Supreme Court strictly applied *Bellas Hess* in its decision, ignoring all the technological, commercial, and legal developments of the last 25 years, which have eviscerated the rationale of *Bellas Hess,* as well as the undisputed facts showing the benefits respondent received from the State.

The Supreme Court of North Dakota has taken the opposite view, not only in result but also in the thorough analysis in its opinion. Whereas the Connecticut Court held that the only reliable test was a simple "bright line" test based entirely upon physical presence in the state, the North Dakota Court recognized the lack of reality in such a strict application of *Bellas Hess:*

> [W]e are mindful that prior cases cannot be read in a vacuum, but must be considered in light of their relevant facts and historical context. (Citations omitted.)
>
> * * *
>
> Quill in effect asks us to accept the notion that the United States Supreme Court will abandon its common sense and experience at the courthouse

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(Continued from previous page)

however, that the better course is to grant its petition now, since the validity of *Bellas Hess* was squarely addressed by the Connecticut Supreme Court, and this Court would have the benefit of North Dakota's opinion in any event. Connecticut also has an interest in prompt resolution of the issue, since its current practice has been held unconstitutional.

> door and ignore the tremendous social, economic, commercial and legal innovations since 1967, and blindly apply an obsolescent precedent.

North Dakota v. Quill, slip op. at 8-9 (App. p. A10).

The Court further stated:

> The economic, social and commercial landscape upon which *Bellas Hess* was premised no longer exists, save perhaps in the fertile imagination of attorneys representing mail order interest.

Id. at 10 (App. p. A11).

The North Dakota Court then goes on to catalog all the changes since 1967 which bear on this issue, including a detailed review of this Court's decisions concerning the Commerce Clause vis-á-vis state taxation. Among the many crucial developments in the last two decades are the tremendous growth of the mail order business and dramatic changes in computer technology, which greatly facilitates recordkeeping by mail order companies.

Another critical issue is whether the state's disposal of tons of catalogs shipped to its residents is a service to the seller or to the recipient. This aspect of the controversy today was not at issue in *Bellas Hess.* The totality of the Connecticut Supreme Court's view is set forth in a two-sentence footnote:

> The commissioner's argument that Folio derives benefit from Connecticut by virtue of the state disposing of the catalogs as paper trash is likewise without merit. Because the catalogs are the property of the Connecticut residents, it is axiomatic that it is the resident who is deriving the benefit from the state and who must contribute to the cost of the disposal.

SFA Folio Collections, Inc. v. Bannon, Commissioner of Revenue Services, 217 Conn. 220, 585 A.2d 666, 671 n.6 (1991).

Again, the contrasting views of the two state high courts is clear from the *Quill* opinion, at 34 (App. p. A34):

> The [Connecticut] court's rationale is far too simplistic. To suggest that the seller derives no benefit from the State's waste-collection efforts because theoretically the catalogs become the consumer's "property" when they reach the mailbox ignores the realities of the situation, and fails to take into account that most mail order solicitations have not been requested, and may in fact be unwanted, by the consumer.

In addition to the diametrically opposed cases from Connecticut and North Dakota, there is a third approach that has prevailed in the trial courts of Tennessee. Where Connecticut steadfastly adheres to *Bellas Hess,* and North Dakota, with forthright candor, declares this precedent as outmoded, the Chancery Court of Tennessee took a middle ground. In *SFA Folio Collections v. Huddleston,* No. 89-3015-III (Ch. Tenn. March 11, 1991), the Court acknowledges that "[w]hile the *Bellas Hess* case is instructive, it does not provide a complete answer to the present case." *Id.* at 2. The Court then goes on to find "no violation of Folio's constitutional rights by the enforcement of [the Tennessee sales and use tax]". *In accord Bloomingdale's By Mail, Ltd. v. Huddleston,* No. 89-3017-II (Ch. Tenn. March 8, 1991), *appeal pending.*

Forty-five states and the District of Columbia have enacted sales and use taxes. CCH *State Tax Handbook* (1990) at 662. Each of these states, with growing fiscal demands, has a keen interest in this Court revisiting its

decision in *Bellas Hess*. This Court should address the question whether *Bellas Hess* is a binding precedent upon the states, as the Connecticut Court held, or "a derelict in the stream of the law," as the North Dakota Court concluded. *Quill*, slip op. at 37 n. 3 (App. p. A37).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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IN THE SUPREME COURT

STATE OF NORTH DAKOTA

FILED BY CLERK
SUPREME COURT MAY 7 1991

State of North Dakota, by and through its Tax Commissioner, Heidi Heitkamp,	Plaintiff, Appellant and Cross-Appellee
v.	
Quill Corporation,	Defendant, Appellee and Cross-Appellant

Civil No. 900257

Appeal from the District Court for Burleigh County, South Central Judicial District, the Honorable Benny A. Graff, Judge.

REVERSED.

Opinion of the Court by VandeWalle, Justice.

Nicholas J. Spaeth, Attorney General, Bismarck, for plaintiff, appellant and cross-appellee.

John E. Gaggini (argued), and Don S. Harnack (appearance), of McDermott, Will & Emery, Chicago, IL, and William P. Pearce (appearance), of Pearce & Durick, Bismarck, for defendant, appellee and cross-appellant.

State v. Quill Corporation

Civil No. 900257

VANDEWALLE, Justice.

The State of North Dakota appealed from a district court summary judgment declaring that subsections (6) and (7) of Section 57-40.2-01, N.D.C.C., are unconstitutional as applied to Quill Corporation [Quill], and that the State therefore may not require Quill to collect and remit use tax on its sales to North Dakota consumers. Quill cross-appealed from that part of the summary judgment dismissing its action under 42 U.S.C. § 1983 and denying attorney's fees under 42 U.S.C. § 1988. We hold that Section 57-40.2-01, N.D.C.C., is constitutional as applied to Quill and accordingly we reverse the summary judgment.

I

Quill is a Delaware corporation with offices and warehouses in Illinois, California and Georgia. Quill sells office supplies, stationery, and equipment, offering over 9,500 different products ranging from paper clips to computers. Its annual sales are in excess of $200,000,000.

Quill solicits business through its numerous catalogs and flyers, advertisements in nationally distributed "card packs," advertisements in national periodicals and trade journals, and telephone solicitation of current customers. Of the more than 200,000 orders Quill receives monthly, approximately one-half are by telephone. The remaining half are received by mail, fax, telex, and by direct computer contact.

Quill's annual sales to nearly 3,500 active[1] North Dakota customers are just under $1,000,000. By sales volume, it is the sixth largest seller of office supplies in North Dakota. Quill each year mails over 60 different catalogs and flyers to its North Dakota customers. This amounts to more than 230,000 separate pieces of mail, weighing over 24 tons, sent into the State annually by Quill.

North Dakota imposes a use tax upon property purchased for storage, use, or consumption within the State. Section 57-40.2-01, N.D.C.C. The rate is equivalent to the corollary sales tax. See Sections 57-39.2-02.1 and 57-40.2-02.1, N.D.C.C. A credit is given if sales or use taxes have been paid to another state upon the same property. Section 57-40.2-11, N.D.C.C.

Although the consumer is ultimately responsible for the tax, a "retailer maintaining a place of business in this state" is required to collect the tax from the consumer and remit it to the State. Section 57-40.2-07, N.D.C.C. Section 57-40.2-01, N.D.C.C., defines "retailer" and "retailer maintaining a place of business in this state":

> "6. 'Retailer' includes every person engaged in the business of selling tangible personal property for use within the meaning of this chapter. . . . A retailer also includes every person who engages in regular or systematic solicitation of a consumer market in this state by the distribution of catalogs, periodicals, advertising flyers, or other advertising, or by means of print, radio or television media, by mail, telegraphy, telephone, computer data base, cable, optic, microwave, or other communication system.

> "7. 'Retailer maintaining a place of business in this state', or any like term, means any retailer having or maintaining within this state, directly or by a subsidiary, an office, distribution house, sales house, warehouse, or other place of business, or any agent operating within this state. . . . It also includes every person who engages in regular or systematic solicitation of sales of tangible personal property in this state by the distribution of catalogs, periodicals, advertising flyers, or other advertising, by means of print, radio or television media, or by mail, telegraphy, telephone, computer data base, cable, optic, microwave, or other communication system for the purpose of effecting retail sales of tangible personal property."

Section 81-04.1-01-03.1(3) of the North Dakota Administrative Code defines "regular or systematic solicitation" as "three or more separate transmittances of any advertisement or advertisements" during a specified twelve-month period.[2]

Quill has refused to collect and remit use taxes on goods purchased and used by Quill's customers in North Dakota. The State, through its Tax Commissioner, commenced this declaratory judgment action under Chapter 32-23, N.D.C.C., seeking a declaration that Quill is a "retailer" and a "retailer maintaining a place of business in this state" which must collect and remit the applicable use tax on its sales to customers in this State.

Quill answered, alleging that Chapter 57-40.2, N.D.C.C., as applied to Quill, is violative of the Due

Process Clause and Commerce Clause of the United States Constitution as interpreted in *National Bellas Hess, Inc. v. Department of Revenue,* 386 U.S. 753, 87 S.Ct. 1389, 18 L.Ed.2d 505 (1967). Quill filed a counterclaim seeking relief under 42 U.S.C. § 1983 for alleged violations of its Due Process and commerce Clause rights, and seeking attorney's fees under 42 U.S.C. § 1988.

On cross-motions for summary judgment, the district court held that the State could not constitutionally require Quill to collect and remit use taxes. Relying principally upon *Bellas Hess,* the district court held that the State had failed to establish a sufficient nexus between Quill and the State, and that subsections (6) and (7) of Section 57-40.2-01 were therefore unconstitutional as applied to Quill. The court dismissed Quill's counterclaim seeking relief under 42 U.S.C. §§ 1983 and 1988.

Judgment was entered accordingly and the State appealed. Quill cross-appealed from that part of the judgment dismissing its counterclaim.

II

A

Quill concedes that its solicitation of sales in North Dakota meets the statutory and administrative guidelines for a "retailer maintaining a place of business in this state." Thus, the dispositive issue on appeal is whether the State may constitutionally require Quill to collect and remit the use tax.

Any discussion of imposition of the duty of collecting a use tax upon an out-of-state seller must begin with an

analysis of *Bellas Hess, supra.* National Bellas Hess was incorporated in Delaware and had its principal place of business in Missouri. Illinois attempted to require National Bellas Hess to collect and remit use tax on mail order sales into that state. The United States Supreme Court summarized the constitutional background:

> "National argues that the liabilities which Illinois has thus imposed violate the Due Process Clause of the Fourteenth Amendment and create an unconstitutional burden upon interstate commerce. These two claims are closely related. For the test whether a particular state exaction is such as to invade the exclusive authority of Congress to regulate trade between the States, and the test for a State's compliance with the requirements of due process in this area are similar. . . . As to the former, the Court has held that 'State taxation falling on interstate commerce *** can only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys.' . . . And in determining whether a state tax falls within the confines of the Due Process Clause, the Court has said that the 'simple but controlling question is whether the state has given anything for which it can ask return.' . . . The same principles have been held applicable in determining the power of a State to impose the burdens of collecting use taxes upon interstate sales. Here, too, the Constitution requires 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.' " *Bellas Hess, supra,* 386 U.S. at 756, 87 S.Ct. at 1391, 18 L.Ed.2d at 508-509 (citations omitted).

Characterizing National Bellas Hess as a mail order seller which did "no more than communicate with customers in the State by mail or common carrier," [*Bellas Hess, supra,* 386 U.S. at 758, 87 S.Ct. at 1392, 18 L.Ed.2d at 510], the Court, in a 6-3 decision, held that this connection with Illinois was insufficient to require National Bellas Hess to collect and remit the use tax. The Court drew a "bright line" distinction between mail order sellers whose only connection with its customers in the taxing state was by common carrier or the United States mail and those with more significant connections with the state.

The Court also stressed the substantial administrative burden upon National Bellas Hess if it were required to collect and remit use taxes to numerous jurisdictions. The Court noted that "[t]he many variations in rates of tax, in allowable exemptions, and in administrative and record-keeping requirements could entangle National's interstate business in a virtual welter of complicated obligations to local jurisdictions." *Bellas Hess, supra,* 386 U.S. at 759-760, 87 S.Ct. at 1393, 18 L.Ed.2d at 510 (footnotes omitted).

Justice Fortas, speaking for the dissenters in *Bellas Hess,* formulated a different approach for analyzing the contacts between a taxing state and an out-of-state seller necessary to satisfy Due Process and Commerce Clause requirements. Justice Fortas suggested a more case-specific approach which would take into consideration the nature and extent of the solicitation and exploitation of the state's consumer market:

"There should be no doubt that this large-scale, systematic, continuous solicitation and exploitation of the Illinois consumer market is a sufficient 'nexus' to require Bellas Hess to collect from Illinois customers and to remit the use tax, especially when coupled with the use of the credit resources of residents of Illinois, dependent as that mechanism is upon the State's banking and credit institutions. Bellas Hess is not simply using the facilities of interstate commerce to serve customers in Illinois. It is regularly and continuously engaged in 'exploitation of the consumer market' of Illinois . . . by soliciting residents of Illinois who live and work there and have homes and banking connections there, and who, absent the solicitation of Bellas Hess, might buy locally and pay the sales tax to support their State. Bellas Hess could not carry on its business in Illinois, and particularly its substantial credit business, without utilizing Illinois banking and credit facilities." *Bellas Hess, supra,* 386 U.S. at 761-762, 87 S.Ct. at 1394, 18 L.Ed.2d at 511-512 (Fortas, J., dissenting) (citations omitted).

Justice Fortas forecast the rationale for the diminishment of the constitutional significance of "physical presence" in such cases:

"Bellas Hess enjoys the benefits of, and profits from the facilities nurtured by, the State of Illinois as fully as if it were a retail store or maintained salesmen therein. Indeed, if it did either, the benefit that it received from the State of Illinois would be no more than it now has – the ability to make sales of its merchandise, to utilize credit facilities, and to realize a profit; and, at the same time, it would be required to pay additional taxes. Under the present arrangement, it conducts its substantial, regular, and systematic business in Illinois and the

> State demands only that it collect from its customer-users – and remit to the State – the use tax which is merely equal to the sales tax which resident merchants must collect and remit. To excuse Bellas Hess from this obligation is to burden and penalize retailers located in Illinois who must collect the sales tax from their customers. In Illinois the rate is 3½%, and when it is realized that in some communities the sales tax requires, in effect, that as much as 5% be added to the amount that customers of local, tax-paying stores must pay, the importance of the competitive discrimination becomes apparent. While this advantage to out-of-state sellers is tolerable and a necessary constitutional consequence where the sales are occasional, minor and sporadic and not the result of a calculated, systematic exploitation of the market, it certainly should not be extended to instances where the out-of-state company is engaged in exploiting the local market on a regular, systematic, large-scale basis. In such cases, the difference between the nature of the business conducted by the mail order house and by the local enterprise is not entitled to constitutional significance." *Bellas Hess, supra,* 386 U.S. at 762–763, 87 S.Ct. at 1394–1395, 18 L.Ed.2d at 512 (Fortas, J., dissenting).

The dissent also disputed the extent of the administrative burden which would be placed upon National Bellas Hess, noting that the majority's stated fear of entanglement of interstate commerce "vastly underestimates the skill of contemporary man and his machines." *Bellas Hess, supra,* 386 U.S. at 766, 87 S.Ct. at 1396, 18 L.Ed.2d at 514 (Fortas, J., dissenting). Justice Fortas therefore concluded that neither the Commerce Clause nor the Due

Process Clause excused National Bellas Hess from complying with the Illinois use tax statutes.

B

The United States Supreme Court has not revisited this precise issue since 1967. While we necessarily begin our analysis in the context of the majority opinion in *Bellas Hess,* we are mindful that prior cases cannot be read in a vacuum, but must be considered in light of their relevant facts and historical context. See *Penry v. Lynaugh,* 492 U.S. 302, 109 S.Ct. 2934, 106 L.Ed.2d 256 (1989) (Scalia, J., concurring in part and dissenting in part). Similarly, appellate review in general is not to be conducted in a vacuum. *Cullen v. Williams County,* 446 N.W.2d 250 (N.D. 1989). Appellate judges bring to each case their common sense, ordinary experience, and observation of human affairs. *Cf. Nebraska Press Association v. Stuart,* 427 U.S. 539, 96 S.Ct. 2791, 49 L.Ed.2d 683 (1976); *Salve Regina College v. Russell,* ____ U.S. ____, 111 S.Ct. 1217, ____ L.Ed.2d ____ (1991) (Rehnquist, C.J., dissenting); *State v. Olmstead,* 261 N.W.2d 880 (N.D.), *cert. denied,* 436 U.S. 918, 98 S.Ct. 2264, 56 L.Ed.2d 759 (1978).

Quill in effect asks us to accept the notion that the United States Supreme Court will abandon its common sense and experience at the courthouse door and ignore the tremendous social, economic, commercial, and legal innovations since 1967, and blindly apply an obsolescent precedent. We have in the past been chided by the United States Supreme Court for doing just that, and in failing to detect changes in legal course by that Court. See *North Dakota State Board of Pharmacy v. Snyder's Drug Stores, Inc.,*

414 U.S. 156, 94 S.Ct. 407, 38 L.Ed.2d 379 (1973), *reversing* 202 N.W.2d 140 (N.D. 1972). See also, *Snyder's Drug Stores, Inc. v. North Dakota State Board of Pharmacy,* 219 N.W.2d 140 (N.D. 1974) (on remand).[3] We are guided by the maxim that "[w]hen the reason of a rule ceases so should the rule itself." Section 31-11-05(1), N.D.C.C. We have little doubt that maxim has wider application than our state boundaries. As noted by Justice Cardozo, "[t]here should be greater readiness to abandon an untenable position when the rule to be discarded may not reasonably be supposed to have determined the conduct of the litigants, and particularly when in its origin it was the product of institutions or conditions which have gained a new significance or development with the progress of the years." Cardozo, The Nature of the Judicial Process 151 (1921) [*quoted in Kitto v. Minot Park District,* 224 N.W.2d 795, 803 (N.D. 1974)].

C

The economic, social, and commercial landscape upon which *Bellas Hess* was premised no longer exists, save perhaps in the fertile imaginations of attorneys representing mail order interests. In the quarter-century which has passed in the interim, "mail order" has grown from a relatively inconsequential market niche into a goliath now more accurately delineated as "direct marketing." The burgeoning technological advances of the 1970's and 1980's have created revolutionary communications abilities and marketing methods which were undreamed of in 1967.[4]

Rather than a few full-line mail order retailers essentially offering a "department store by mail," mail order is today marked by literaliy thousands of specialized catalogs targeted at specific groups of consumers. Technology has triggered this transformation, with computerized database marketing allowing mailings directed to specific demographical groups. In fact, the sale and rental of lists of names of prior or potential mail order purchasers has itself become a three-billion-dollar business.[5] Technology has also changed the method of receiving orders, with the increased efficiency of toll-free telephone lines, fax orders, and direct computer ordering replacing the less-immediate "mail" order, and advances in the parcel delivery industry allow a wide variety of options, including overnight delivery.

Perhaps the greatest change in mail order since 1967 has been in terms of sheer volume. Gone are the days of the Spring and Fall Sears catalog being the definition of mail order. It is estimated that in 1990 13.6 *billion* catalogs were mailed to consumers in the United States, an increase of 7.8 billion in ten years. Over 54 percent of Americans – 98 million – made a mail order purchase, an increase of 40 million since 1983.[6] Mail order sales, in the neighborhood of $2.4 billion in 1967 [*see Bellas Hess, supra,* (Fortas, J., dissenting)], reached the staggering figure of $183.3 billion in 1989.[7] By the mid-1980's, mail order accounted for more than 15 percent of total sales nationally. See, e.g., 43 Cong. Q. 2571 (Dec. 7, 1985); Hartman, *Collection of the Use Tax on Out-of-State Mail-Order Sales,* 39 Vand.L.Rev. 993 (1986).

While in 1967 it may have generally been necessary to rely upon in-state sales personnel and inventory to successfully market a product, technology has changed the rules of the game. Today a direct marketer can communicate with his customers across the country through toll-free incoming telephone lines, national WATS telephone service, fax machines, telex, or direct computer communication just as effectively, and more efficiently, than if he were calling personally on each customer. Clearly the direct marketing of the 1990's bears little resemblance to the mail order of the 1960's.

D

Just as the changes in marketing techniques have affected the economic and commercial landscape since *Bellas Hess,* so too has the legal landscape been altered in that quarter-century.[8] The Supreme Court's expansion of state authority to tax interstate commerce, as well as its broadening of other areas of Due Process and Commerce Clause analysis, leads us to conclude that the foundational basis of *Bellas Hess* has been eroded and that the Supreme Court would so conclude.

Perhaps the most striking shift in the Court's position on taxation of interstate commerce occurred in *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977), in which the Court overruled years of precedent and developed a four-prong test to assess Commerce Clause challenges to state taxation of interstate commerce. Prior to that time, Commerce Clause analysis was controlled by the free trade view, as enunciated in *Spector Motor Service v. O'Connor,* 340 U.S. 602, 71

S.Ct. 508, 95 L.Ed. 573 (1951), that direct taxation of interstate commerce was *per se* unconstitutional. See P. Hartman, Federal Limitations on State and Local Taxation §§ 2:16, 2:17 (1981) [hereafter "Hartman, Federal Limitations"]; Recent Developments, *D.H. Holmes Co. v. McNamara: Use Tax on Catalogs Does Not Violate Commerce Clause,* 63 Tul. L. Rev. 407 (1988). Thus, at the time of *Bellas Hess,* Commerce Clause analysis often focused upon whether the challenged tax was levied upon the privilege of doing interstate business or upon some other less-direct incidence of interstate commerce.

The *Spector* doctrine was widely criticized as dependent upon illusory distinctions, legislative labelling, and insubstantial and pointless formalism. Hartman, Federal Limitations, *supra,* at §§ 2:16–2:17; see also, *Complete Auto, supra;* McCray, *Commerce Clause Sanctions Against Taxation on Mail Order Sales: A Re-Evaluation,* 17 Urb. Law. 529 (1985); Recent Developments, 63 Tul. L. Rev. 407, *supra.* The Court, noting that the *Spector* rule "has no relationship to economic realities" and "stands only as a trap for the unwary draftsman," *Complete Auto, supra,* 430 U.S. at 279, 97 S.Ct. at 1079, 51 L.Ed.2d at 331, specifically overruled *Spector* and announced a four-prong test for evaluating Commerce Clause challenges to state taxation. Under the *Complete Auto* formulation, a tax does not violate the Commerce Clause if it (1) is applied to an activity with a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to the services provided by the state. *Complete Auto, supra;* see also, *Trinova Corp. v. Michigan Department of Treasury,* ____ U.S. ____, 111 S.Ct. 818, 112 L.Ed.2d 884 (1991); *D.H. Holmes Co. v.*

McNamara, 486 U.S. 24, 108 S.Ct. 1619, 100 L.Ed.2d 21 (1988).

One month after deciding *Complete Auto,* the Court expanded the authority of the states to require out-of-state sellers to collect and remit a use tax in *National Geographic Society v. California Board of Equalization,* 430 U.S. 551, 97 S.Ct. 1386, 51 L.Ed.2d 631 (1977). National Geographic sold maps, atlases, globes, and books by mail order to California residents. National Geographic had two offices in California which solicited advertising for its magazine, but which performed no activities related to the mail order sales. National Geographic challenged California's authority to require collection of use tax on its mail order sales, alleging that there was insufficient nexus between its mail order sales and California.

In prior cases, including *Complete Auto,* the Court had phrased the nexus requirement in terms of the relationship between the taxing state and the *activity* to be taxed. In *National Geographic,* however, the Court expanded the concept of nexus in use tax cases to situations where the out-of-state *seller* has the requisite nexus with the taxing state. Thus, the Court focused upon the benefits and services provided by the state to National Geographic's two advertising offices to support collection of use tax upon its unrelated mail order sales into the state.

In so holding, the Court stressed the distinction between the lesser burdens placed upon the seller by a use tax, which is ultimately borne by the in-state purchaser, and a more direct tax upon the seller:

> "Other fairly apportioned, nondiscriminatory direct taxes have also been sustained when the taxes have

> been shown to be fairly related to the services provided the out-of-state seller by the taxing State. . . .
>
> "The case for the validity of the imposition upon the out-of-state seller enjoying such services of a duty to collect a use tax is even stronger. . . . The out-of-state seller runs no risk of double taxation. The consumer's identification as a resident of the taxing State is self-evident. . . . The out-of-state seller becomes liable for the tax only by failing or refusing to collect the tax from that resident consumer. Thus, the sole burden imposed upon the out-of-state seller by statutes like §§ 6203 and 6204 is the administrative one of collecting it." *National Geographic, supra,* 430 U.S. at 558, 97 S.Ct. at 1391, 51 L.Ed.2d at 638 (citations omitted).

Thus, the Court not only expanded the concept of nexus, but it also recognized the purely administrative nature of the collection duty in use tax cases and indicated that a lesser showing of nexus may suffice in such cases.

More recently, in a case presenting an interesting twist to the usual use tax situation, the Court upheld imposition of use taxes upon catalogs themselves in *D.H. Holmes Co. v. McNamara, supra.* Holmes, which had thirteen stores in Louisiana, had its catalogs printed out-of-state and mailed from those locations directly to Louisiana customers. The catalogs promoted items available for sale in the local stores, and also could be used to order items by mail. Louisiana sought to collect from Holmes use taxes based upon the value of the catalogs, asserting that they were "used" by Holmes within the state.

The Court applied the *Complete Auto* test and upheld imposition of the tax. Most importantly for our purposes, the Court distinguished *Bellas Hess* in holding that Holmes had sufficient nexus with Louisiana. Although, as the Court noted, there was " 'nexus' aplenty" present, *Holmes, supra,* 486 U.S. at 33, 108 S.Ct. at 1624, 100 L.Ed.2d at 29, what is particularly noteworthy is the language employed by the Court to distinguish *Bellas Hess.* Notwithstanding that Holmes was incorporated in Louisiana, had its registered office there, and had thirteen stores with 5,000 employees in the state, the first factor noted by the Court in distinguishing *Bellas Hess* was "Holmes' significant *economic* presence in Louisiana." *Holmes, supra,* 486 U.S. at 33, 108 S.Ct. at 1624, 100 L.Ed.2d at 29 (emphasis added). In a case involving obvious physical presence, we find it significant that the Court chose to stress economic presence, the phraseology of the *Bellas Hess* dissent.

The Court has also discussed the broadening concept of nexus in cases involving constitutional challenges to other taxes upon interstate commerce. For example, in *Standard Pressed Steel Co. v. Washington Department of Revenue,* 419 U.S. 560, 95 S.Ct. 706, 42 L.Ed.2d 719 (1975), a manufacturer of industrial and aerospace fasteners challenged imposition of Washington's business and occupation tax levied upon its unapportioned gross receipts from sales in the state. Standard Pressed Steel's sole connection with the state, other than its interstate sales, was one employee, working from his home in the state, who serviced the company's one large account in the state, the Boeing Company. This employee was a consultant only; he did not take orders on behalf of Standard.

Rather than focusing upon Standard's minimal physical contact with the state through a single employee, and the concomitant minimal benefits and services provided to the company, the Court instead emphasized the connection between the employee's activities and the establishment and continuance of sales to Boeing. In other words, instead of relying upon a bright-line demarcation based upon Standard's physical presence in the taxing state and the receipt of benefits and services, the Court in finding nexus stressed that the employee "made possible the realization and continuance of valuable contractual relations between [Standard] and Boeing" [*Standard Pressed Steel, supra,* 419 U.S. at 562, 95 S.Ct. at 708, 42 L.Ed.2d at 722], and that the employee's "services were substantial 'with relation to the establishment and maintenance of sales, upon which the tax was measured.' " *Standard Pressed Steel, supra,* 419 U.S. at 563, 95 S.Ct. at 709, 42 L.Ed.2d at 723 (*quoting General Motors Corp. v. Washington,* 377 U.S. 436, 447, 84 S.Ct. 1564, 1571, 12 L.Ed.2d 430, 439 (1964), *overruled on other grounds, Tyler Pipe Industries, Inc. v. Washington State Department of Revenue,* 483 U.S. 232, 107 S.Ct. 2810, 97 L.Ed.2d 199 (1987)). In so holding, the Court stated that Standard's asserted lack of nexus "verges on the frivolous." *Standard Pressed Steel, supra,* 419 U.S. at 562, 95 S.Ct. at 708, 42 L.Ed.2d at 722.

In *Tyler Pipe, supra,* the Court was again presented with a nexus challenge to the Washington business and occupation tax. Tyler Pipe had one representative soliciting business in state, but, in contrast to *Standard Pressed Steel, supra,* Tyler Pipe's salesman was an independent contractor, not an employee. The Court, relying upon *Scripto,*

Inc. v. Carson, 362 U.S. 207, 80 S.Ct. 619, 4 L.Ed.2d 660 (1960), held that the salesman's status as an independent contractor was without constitutional significance. Concluding that the activities of the independent contractor within the state created a sufficient nexus to support imposition of the tax, the Court agreed with the Washington Supreme Court that " 'the crucial factor governing nexus is whether the activities performed in this state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales.' " *Tyler Pipe, supra,* 483 U.S. at 250, 107 S.Ct. at 2821, 97 L.Ed.2d at 215-216 (*quoting Tyler Pipe Industries, Inc. v. State,* 105 Wash.2d 318, 323, 715 P.2d 123, 126 (1986)). Thus, in both *Standard Pressed Steel* and *Tyler Pipe,* the Court did not employ a bright-line physical presence test, but instead focused upon the relationship between the out-of-state seller's contacts with the state and its establishment and maintenance of sales within the state.

While the Court has been expanding states' authority to tax interstate commerce, it has also significantly broadened the closely related Due Process analysis in personal jurisdiction cases. In *Burger King Corp. v. Rudzewicz,* 471 U.S. 462, 472-473, 105 S.Ct. 2174, 2182, 85 L.Ed.2d 528, 540-541 (1985), the Court summarized some examples of conduct which will satisfy the minimum contacts requirement and justify assertion of personal jurisdiction over an out-of-state seller:

> "Where a forum seeks to assert specific jurisdiction over an out-of-state defendant who has not consented to suit there, this 'fair warning' requirement is satisfied if the defendant has 'purposefully

> directed' his activities at residents of the forum . . . and the litigation results from alleged injuries that 'arise out of or relate to' those activities. . . . Thus '[t]he forum State does not exceed its powers under the Due Process Clause if it asserts personal jurisdiction over a corporation that delivers its products into the stream of commerce with the expectation that they will be purchased by consumers in the forum State' and those products subsequently injure forum consumers. . . . Similarly, a publisher who distributes magazines in a distant State may fairly be held accountable in that forum for damages resulting there from an allegedly defamatory story. . . . And with respect to interstate contractual obligations, we have emphasized that parties who 'reach out beyond one state and create continuing relationships and obligations with citizens of another state' are subject to regulation and sanctions in the other State for the consequences of their activities. . . ." (Citations omitted.)

It is clear that Quill has "purposefully directed" its activities at North Dakota residents, has "reach[ed] out . . . and create[d] continuing relationships and obligations with citizens" of this State, and has gone beyond placing its products into a general stream of commerce – it has sold and delivered its products directly to North Dakota consumers. It is therefore clear that Quill could, consistent with Due Process, be brought into a North Dakota court to litigate claims arising from those activities.

More significant, however, is the Court's clear recognition that technological advances have made physical presence within the jurisdiction meaningless in modern commerce:

> "Jurisdiction in these circumstances may not be avoided merely because the defendant did not *physically* enter the forum State. Although territorial presence frequently will enhance a potential defendant's affiliation with a State and reinforce the reasonable foreseeability of suit there, it is an inescapable fact of modern commercial life that a substantial amount of business is transacted solely by mail and wire communications across state lines, thus obviating the need for physical presence within a State in which business is conducted. So long as a commercial actor's efforts are 'purposefully directed' toward residents of another State, we have consistently rejected the notion that an absence of physical contacts can defeat personal jurisdiction there." *Burger King, supra,* 471 U.S. at 476, 105 S.Ct. at 2184, 85 L.Ed.2d at 543.

The Court also recognized the unfairness which would result if out-of-state sellers were allowed to wholly escape responsibility for the consequences of their actions in other states:

> "Moreover, where individuals 'purposefully derive benefit' from their interstate activities . . . it may well be unfair to allow them to escape having to account in other States for consequences that arise proximately from such activities; the Due Process Clause may not readily be wielded as a territorial shield to avoid interstate obligations that have been voluntarily assumed. And because 'modern transportation and communications have made it much less burdensome for a party sued to defend himself in a State where he engages in economic activity,' it usually will not be unfair to subject him to the burdens of litigating in another forum for disputes relating to such activity. . . ." *Burger King,*

supra, 471 U.S. at 473-474, 105 S.Ct. at 2183, 85 L.Ed.2d at 541 (citations omitted).

E

In light of these wholesale changes in the social, economic, commercial, and legal arenas, we are required to apply *Bellas Hess* in a contemporary context as we believe the Supreme Court would apply that decision.

The Supreme Court has recently recognized that sweeping technological changes may require corresponding changes in legal doctrine. In *Goldberg v. Sweet,* 488 U.S. 252, 109 S.Ct. 582, 102 L.Ed.2d 607 (1989), Illinois' telecommunications excise tax was challenged on Commerce Clause grounds. After a lengthy discussion of the "explosion in new telecommunications technologies" [*Goldberg, supra,* 488 U.S. at 255, 109 S.Ct. at 585, 102 L.Ed.2d at 613], the Court concluded that "Illinois' method of taxation is a realistic legislative solution to the technology of the present-day telecommunications industry." *Goldberg, supra,* 488 U.S. at 265, 109 S.Ct. at 591, 102 L.Ed.2d at 619. Commenting on prior cases striking down similar state taxes on interstate telecommunications, the Court simply noted that "[t]hese cases considered a telecommunications technology only distantly related to modern telecommunications technology and were decided in a pre-*Complete Auto* era when this Court held the view that interstate commerce itself could not be taxed." *Goldberg, supra,* 488 U.S. at 265 n.16, 109 S.Ct. at 591 n.16, 102 L.Ed.2d at 619 n.16.

Similarly, the Court in *Burger King, supra,* 471 U.S. at 476, 105 S.Ct. at 2184, 85 L.Ed.2d at 543, noted the

technological changes which have affected modern commerce: "[I]t is an inescapable fact of modern commercial life that a substantial amount of business is transacted solely by mail and wire communications across state lines, thus obviating the need for physical presence within a State in which business is conducted." In *Goldberg* and *Burger King* the Court has recognized that legal theory must be flexible to account for societal changes, and that the vast technological explosion of recent years often requires rethinking of previous doctrine. We therefore are instructed to be cognizant of the vast differences between the mail order of the 1960's and the direct marketing of the 1990's when applying *Bellas Hess* in this case. In addition, the *Bellas Hess* majority specifically characterized the transactions there as being carried out only by mail or common carrier. Very little of the direct marketing of today is limited to mail or common carrier, and the facts of this case clearly demonstrate that Quill's business extended far beyond those limited circumstances.

We also recognize the Court's extensive shift in focus in interstate commerce tax cases. The Court has wholly rewritten the underlying theory in such cases and formulated a new test to measure Commerce Clause challenges. See *Complete Auto, supra.* In *National Geographic, supra,* the Court stressed the administrative nature of the use tax collection requirement and held that a lower threshold of nexus may suffice in use tax cases than in attempts to collect a tax directly from the out-of-state seller. In *Holmes, supra,* the Court applied the *Complete Auto* test to judge a use tax and noted the seller's significant economic presence within the taxing state to find sufficient nexus and distinguish *Bellas Hess.*

Complete Auto and subsequent interstate commerce tax cases have been viewed as an abandonment of the Court's previous formalistic approach in favor of a "more realistic functional calculus" [L. Tribe, American Constitutional Law § 6-15, at 441 (2d ed. 1988)], "grounded in practicality and economic reality" [Recent Developments, 63 Tul. L. Rev. 407, *supra*]. See also, *Trinova Corp. v. Michigan Department of Treasury, supra; Mobil Oil Corp. v. Commissioner of Taxes of Vermont,* 445 U.S. 425, 100 S.Ct. 1223, 63 L.Ed.2d 510 (1980). The Court's opinions in *Standard Pressed Steel* and *Tyler Pipe* also demonstrate a greater emphasis upon the economic consequences and realities of the transactions at issue rather than a bright-line physical presence test. Although in each of these cases there was some degree of physical presence within the taxing state, the Court's analysis evinces a retreat from the formalistic constrictions of a stringent physical presence test in favor of a more flexible substantive approach. Accordingly, we believe that a contemporary view of nexus is not dependent upon rigid benchmarks to be applied across the board, but requires a review of the totality of the circumstances, on a case-by-case basis, with special emphasis upon the economic realities presented. See Hartman, *Collection of the Use Tax, supra.* This approach best comports with the Court's current Due Process and Commerce Clause analysis.

We are particularly mindful of the illogical results which can flow from a strict requirement of physical presence within the taxing state in light of the contemporary legal and commercial landscape. For example, a small out-of-state seller with minimal sales in the taxing state solicited through an independent-contractor travel-

ing salesperson would have sufficient nexus to support a duty to collect and remit the use tax [see *Tyler Pipe, supra,* and *Scripto, supra*], yet a mail order leviathan with millions of dollars of annual sales solicited by innumerable catalogs and flyers, and consummated by telephone, fax, telex, or direct computer contact, would be deemed unreachable because it has insufficient nexus with the state. Such a result merely propounds the legal fiction that the fire and police protection provided to one salesperson hawking wares in the state provides a more significant "benefit" than does creating and maintaining a social and commercial climate that enables the out-of-state seller to exploit the state's consumer market to the tune of millions of dollars. See, e.g., Hartman, *Collection of the Use Tax, supra;* Simet, *The Concept of "Nexus" and State Use and Unapportioned Gross Receipts Taxes,* 73 Nw.U.L.Rev. 112 (1978).

The Court's current personal jurisdiction analysis also strongly suggests a retrenchment from physical presence as a benchmark in Due Process analysis. A corporation that merely delivers its product into the stream of commerce with the expectation that it will be purchased by a consumer in another state may be subjected to litigation there *[Burger King, supra],* yet Quill asserts that subjecting it to collection of the use tax, in spite of its continuous, intentional, and massive exploitation of this State's consumer market, would be violative of Due Process. It would be illogical indeed to hold that Quill, which could clearly be haled into a North Dakota court if one of its products injured a North Dakota consumer, could not be saddled with the purely *administrative* burden of collecting a use tax. See *National Geographic, supra.*

Finally, we note with irony in Quill's reliance upon the Due Process Clause and the Commerce Clause in seeking to maintain a tax-free mail order haven and thereby retain an economic advantage over its local competitors.[9] The touchstone of Due Process is fundamental fairness. *Burger King, supra; Bearden v. Georgia,* 461 U.S. 660, 103 S.Ct. 2064, 76 L.Ed.2d 221 (1983). The "very object" of the Commerce Clause is protection of interstate commerce from discriminatory local practices. *Welton v. Missouri,* 91 U.S. (1 Otto) 275, 280, 23 L.Ed. 347, 349 (1875); see also, L. Tribe, American Constitutional Law, *supra,* at § 6-17. However, rather than employing the Commerce Clause as a shield against unfair, discriminatory practices favoring local merchants, Quill now raises the Commerce Clause as a sword to carve out a tax-free mail order niche and gain an unfair competitive advantage over local retailers. It would be odd indeed if we were to hold that out-of-state sellers may invoke the Due Process Clause to promote a fundamentally unfair economic advantage over local sellers.

We conclude that Quill's asserted lack of physical presence is not fatal to the State's attempt to require Quill to collect and remit use tax on its sales into North Dakota. Applying *Bellas Hess* in light of subsequent case law, and within the context of contemporary society and commercial practice, we conclude that the concept of nexus encompasses more than mere physical presence within the state, and that the determination of nexus should take into consideration all connections between the out-of-state seller and the state, all benefits and opportunities provided by the state, and should stress economic realities rather than artificial benchmarks.

F

The Court in *Bellas Hess* also focused upon the "virtual welter of complicated obligations" which would be imposed upon mail order sellers if they were required to collect and remit use taxes in every state. *Bellas Hess, supra,* 386 U.S. at 760, 87 S.Ct. at 1393, 18 L.Ed.2d at 510. This basis for the Court's holding has also been seriously eroded by the technological advances of the past quarter-century. The almost universal usage of automated accounting systems, and corresponding advancements in computer technology, have greatly alleviated the administrative burdens created by such a collection duty. See, e.g., Hartman, Federal Limitations, *supra,* at § 10:8; Hartman, *Collection of the Use Tax, supra;* McCray, *Overturning Bellas Hess: Due Process Considerations,* 1985 B.Y.U.L.Rev. 265 (1985).

In addition, in subsequent use tax cases the Supreme Court has all but ignored the burdensome nature of imposition of the collection duty. Furthermore, the Supreme Court has never struck down a use tax solely because of the administrative burdens placed upon the out-of-state seller if sufficient nexus has first been found.

Finally, we note that the seller is allowed to retain a percentage of the use taxes collected as reimbursement for expenses incurred in collecting and remitting the tax. Section 57-40.2-07.1, N.D.C.C. This further alleviates any burdens created by requiring Quill to collect and remit the tax.

We conclude that the burdensome nature of the use tax collection duty does not prohibit imposition of this duty upon Quill in this case.[10]

III

We now turn to the specifics of Quill's constitutional challenge in this case.

All legislative enactments are imbued with a strong presumption of constitutionality, and this presumption is conclusive unless it is clearly shown that the statute contravenes the state or federal constitution. *North Dakota Council of School Administrators v. Sinner,* 458 N.W.2d 280 (N.D. 1990). The party challenging the constitutionality of a statute has the burden of proving its constitutional infirmity. *Best Products Co., Inc. v. Spaeth,* 461 N.W.2d 91 (N.D. 1990); *Newman Signs, Inc. v. Hjelle,* 268 N.W.2d 741 (N.D. 1978), *appeal dismissed,* 440 U.S. 901, 99 S.Ct. 1205, 59 L.Ed.2d 449 (1979). Any doubt must be resolved in favor of the constitutionality of the statute. *North Dakota Council of School Administrators, supra.*

Commerce Clause challenges to use taxes are reviewed under the *Complete Auto* test. See *Holmes, supra.* The only prong of the *Complete Auto* test raised by Quill is the nexus requirement.[11] This first prong is closely related to the fourth prong of *Complete Auto,* which requires that the tax be fairly related to the benefits, opportunities, or services provided by the taxing state. Nexus has historically been analyzed as whether the state has provided some protection, opportunity, or benefit for which it can expect a return. See, e.g., *Bellas Hess, supra; Wisconsin v. J.C. Penney Co.,* 311 U.S. 435, 61 S.Ct. 246, 85 L.Ed. 267 (1940). Thus, we necessarily consider these two related prongs in determining the constitutionality of the use tax as applied to Quill.[12]

The Supreme Court has clarified that the Due Process requirement of a "minimal connection" to establish nexus is encompassed within the *Complete Auto* test. *Trinova Corp. v. Michigan Department of Treasury, supra; Amerada Hess Corp. v. Director, Division of Taxation,* 490 U.S. 66, 109 S.Ct. 1617, 104 L.Ed.2d 58 (1989). Thus, if the tax satisfies the nexus requirement of the *Complete Auto* test, it a fortiorari satisfies the Due Process nexus requirement. *Amerada Hess, supra.*

As discussed in previous sections of this opinion, current Due Process and Commerce Clause analyses indicate that lack of physical presence within the taxing state is not the sole determinative factor in analyzing nexus questions. Rather, we must review all of Quill's contacts with the State to determine whether Quill has a sufficient nexus to satisfy constitutional standards.

Quill's activities directed toward North Dakota consumers clearly establish a substantial "presence" within the State. To iterate Quill's activities, it has 3,500 active customers in North Dakota, and its annual sales of nearly $1,000,000 make it the sixth largest seller of office supplies in the State. It annually mails over 60 different catalogs and flyers to its North Dakota customers, accounting for 230,000 separate pieces of mail. Quill also has a "help line" for consumers to call if they have questions or problems with merchandise ordered from Quill, and specialized service representatives are available to assist with custom printing orders or to answer questions about computers available from Quill. Quill has availed itself of modern technology to engage in an extensive, continuous, and intentional solicitation and exploitation of the

State's consumer market and has thereby established an ubiquitous presence in the State.

Quill has a further connection with North Dakota which supports a finding of nexus. Quill licenses to some of its North Dakota customers a computer software program, Quill Service Link ["QSL"], which permits customers direct computer access to Quill's computer. This allows customers to check Quill's available inventory, confirm current price, and order merchandise directly by computer. Customers with QSL can also communicate with Quill and other customers through an electronic "bulletin board."

Quill retains all rights in QSL through the license agreement. Quill also retains the right to terminate the license "forthwith without prior notice and without cause," and upon termination the customer must "immediately return Software, and copies thereof and the user documentation to Quill." The explicit terms of the licensing agreement belie Quill's assertion that it merely sells the software – lock, stock, and barrel – to the customer. Through its licensing agreement, Quill clearly retains rights to property situated in North Dakota,[13] providing further nexus with the State. See *Matter of Heftel Broadcasting Honolulu, Inc.*, 57 Hawaii 175, 554 P.2d 242 (1976), *cert. denied*, 429 U.S. 1073, 97 S.Ct. 811, 50 L.Ed.2d 791 (1977).

Quill asserts, however, that the State has provided no protections, benefits, or opportunities which justify imposition of the duty to collect and remit the use tax. Quill would have us limit our consideration to solely property-protection functions of the State, such as fire and police

protection, in determining whether the State has given something for which it may ask a return. However, just as the Court's cases of the past 25 years have broadened the concept of nexus, so too have recent cases suggested an expanding view of the benefits which may support State taxation. See, e.g., *Goldberg, supra; Holmes, supra.* Such intangible factors as the benefit of a trained work force and the "other advantages" of a civilized society have been cited by the Court to support imposition of taxes. See, e.g., *Amerada Hess, supra; Goldberg, supra; Holmes, supra.* The Court, in upholding a tax on an out-of-state seller, has also noted Justice Holmes' declaration that "government is the prerequisite for the fruits of civilization for which . . . we pay taxes," and that, accordingly, it was the state that had made the seller's earnings possible. *Wisconsin v. J.C. Penney Co., supra,* 311 U.S. at 446, 61 S.Ct. at 250, 85 L.Ed. at 271.

Various commentators have noted that the benefits and opportunities considered in determining nexus should include economic benefits and opportunities conferred by the State. See, e.g., Hartman, Federal Limitations, *supra,* at §§ 2:7 and 10:8; Hartman, *Collection of the Use Tax, supra;* McCray, *Overturning Bellas Hess, supra;* Simet, *The Concept of "Nexus," supra;* Note, *Imposition of the Duty to Collect State Use Taxes: Constitutional Prohibitions Are No Longer Valid in Mail Order Sales,* 32 S.D.L.Rev. 93 (1986). The underlying rationale is that these benefits and opportunities bear a more direct relationship to the generation of sales for the mail order seller than the comparatively inconsequential benefits and protections provided for a seller's property or personnel within the State. Whether or not an out-of-state seller has a physical presence within

the State, it is the in-state infrastructure which creates and maintains the consumer market and economic climate that fosters demand for the seller's goods and services.

The theory has been summarized by Professor Emeritus Hartman:

> "An unrealistic facet of the *Bellas Hess* doctrine is that the Court presumably thought that a few 'warm bodies' in the taxing state – either operating from an office, or traipsing around hawking their wares without any in-state office – constitute a more satisfactory nexus with a state, for constitutional purposes, than other more substantial and meaningful connections. Benefits from the taxing state that are unrelated to physical contact with the state may be of vastly greater significance than those derived from the presence of a whole swarm of the out-of-state seller's agents soliciting business. Practically speaking, some form of physical presence within the state in furtherance of a business purpose is not essential to the existence of a meaningful nexus with the state. . . .
>
> "For use tax collection purposes, the connection or nexus between the taxing state and out-of-state mail-order sellers should be an economic, rather than physical, relationship. When an out-of-state mail-order seller, for the purpose of realizing a profit, takes advantage of the taxing state's economic climate and milieu through systematic, continuous, and large-scale solicitation of that state's consumer market, that activity should constitute a connection or nexus sufficient to require the out-of-state seller to collect the use tax. When the state provides a substantial economic benefit to the production of income for the out-of-state seller, the

taxing state should be able to demand a tithe from the seller." Hartman, *Collection of the Use Tax, supra,* 39 Vand.L.Rev. at 1013-1014.

Other benefits provided by the state to the mail order seller have also been noted:

"[I]f the buyer is a typical mail order consumer who remains passive in a transaction and does not enter the seller's state, actively initiate contact, negotiate substantial terms of a transaction, or undertake on-going business relationships with the seller, he is not deemed subject to the jurisdiction of the seller's state in a breach of contract action. Sellers are also prohibited from bringing suits in their own states against out-of-state buyers because of a Federal Trade Commission order enjoining such suits as unfair trade practices. A mail order seller may thus enforce his legal rights against a delinquent or fraudulent buyer *only* in the courts of the buyer's state. Thus it is the buyer's state that protects the revenues of the out-of-state seller.

"The buyer's state also benefits the seller by assuring him an orderly market through consumer protection and usury laws on mail order transactions. Such laws create consumer confidence and eliminate unscrupulous sellers from the market. Consumer confidence is critically important to sales which cross state lines. In mail order transactions, consumers must rely heavily on state enforcement mechanisms to rectify wrongs and enforce rights." McCray, *Overturning Bellas Hess, supra,* 1985 B.Y.U.L.Rev. at 285.

An additional indispensable service is provided by the State: it disposes of the 24 tons of solid waste contributed annually to North Dakota landfills by Quill's catalogs and

flyers. Although a similar argument was recently rejected in *SFA Folio Collections, Inc. v. Bannon*, 217 Conn. 220, 585 A.2d 666 (1991), we do not find the reasoning of that case persuasive. The court's discussion of the issue, in total, states:

> "The commissioner's argument that Folio derives benefit from Connecticut by virtue of the state disposing of the catalogs as paper trash is likewise without merit. Because the catalogs are the property of the Connecticut residents, it is axiomatic that it is the resident who is deriving the benefit from the state and who must contribute to the cost of the disposal." *SFA Folio Collections, Inc., supra*, 585 A.2d at 671 n.6.

The court's rationale is far too simplistic. To suggest that the seller derives no benefit from the State's waste-collection efforts because theoretically the catalogs become the consumer's "property" when they reach the mailbox ignores the realities of the situation, and fails to take into account that most mail order solicitations have not been requested, and may in fact be unwanted, by the consumer.[14] It is the mail order seller who derives the most direct benefit from its own mailings, and it therefore is not unreasonable to assume that the seller derives some measure of benefit from the entity that is ultimately responsible for disposing of the veritable mountain of trash created thereby.[15] Certainly the benefit is as direct and consequential as the benefits provided by fire and police protection afforded to an independent contractor solicitor within the state, which have been found sufficient to uphold taxation. See *Tyler Pipe, supra*.

In response to the Connecticut court's rationale it might also be pointed out that, even if we accept the argument that catalogs and flyers become the consumer's property when they are received and that the consumer must therefore contribute to the cost of their disposal, it is the consumer, not the out-of-state seller, who bears the ultimate burden of the use tax. The benefit that the mail order seller receives through the waste collection and disposal services of the state are certainly direct enough to support imposition of the purely administrative burden of collecting and remitting the use tax. See *National Geographic, supra.*

Quill also derived other benefits from the State. Because Quill retained ownership rights in its QSL software and accompanying user documentation, Quill received fire and police protection for its property within the State. The record also demonstrates that Quill contacted North Dakota financial institutions to check credit information on customers, an activity furthered by State regulation of the banking industry.

We conclude that Quill's significant economic presence within the State and its retained ownership of property within the State generate a constitutionally sufficient nexus to justify imposition of the purely administrative duty of collecting and remitting the use tax. We also conclude that the State provides benefits, services, and opportunities which significantly aid Quill's business and which are related to the use tax. Accordingly, the use tax as applied to Quill satisfies the four-prong test of *Complete Auto* and does not violate the Due Process Clause or the Commerce Clause.

Because we hold that the State may constitutionally require Quill to collect and remit use tax on its North Dakota sales, the State's conduct provides no basis for relief under 42 U.S.C. §§ 1983 and 1988. It is therefore unnecessary to address Quill's cross-appeal.

The judgment of the district court is reversed and we remand for entry of a judgment declaring that Quill is a "retailer maintaining a place of business in this state" required to collect and remit use tax in accordance with Chapter 57-40.2, N.D.C.C.

/s/ Gerald W. VandeWalle
/s/ Beryl J. Levine
/s/ [signature illegible]
/s/ [signature illegible]
/s/ [signature illegible]

ENDNOTES

[1] Quill describes an "active" customer as one who has purchased from Quill within the past 24 months.

[2] Section 81-04.1-01-03.1, N.D.A.C., inexplicably states that the definitions therein apply to subsection 5 of Section 57-40.2-01, N.D.C.C. However, the definitions in the Administrative Code section have no logical relationship to subsection 5, and it is therefore apparent that this is an erroneous reference. The parties have not raised this as an issue.

[3] The United States Supreme Court stated that its opinion in an earlier case, upon which we had relied in holding unconstitutional a state statute, was "a derelict in the stream of the law." *North Dakota State Board of Pharmacy v. Snyder's Drug Stores, Inc., supra,* 414 U.S. at 167, 94 S.Ct. at 414, 38 L.Ed.2d at 387. Significantly, in overruling its prior case, the Court quoted with approval the dissent in the earlier case. See *North Dakota State Board of Pharmacy v. Snyder's Drug Stores, Inc., supra;* see also, *Snyder's Drug Stores, Inc. v. North Dakota State Board of Pharmacy, supra,* 219 N.W.2d at 146.

[4] Anyone with a telephone, television, or mailbox can attest to these modern marketing miracles. When you turn on your television set to one of the myriad of available cable channels, you are likely to see numerous commercials for products, "not available in any store," which must be ordered "before midnight tonight" by dialing the toll-free "800" number on the screen. If the commercials are not enough, you may find yourself watching a thirty-minute "infomercial" hawking items as diverse as cosmetics, car wax, weight loss plans, or cooking utensils. If you are a truly modern consumer, you may turn to one of the 24-hour home shopping channels, available on most cable systems, for a continuous opportunity to buy in the comfort of your living room.

The salesperson who calls on the telephone is likely to be armed with significant background information, including your age, occupation, ages of your children, and your hobbies and buying habits, so that sales calls can be specifically targeted to those customers statistically inclined to purchase certain

products. Or, if you prefer, through the wonders of technology you can browse through a computer "catalog," check availability and price of the item you want, and place your order directly through the seller's computer across the country.

The revolution in direct marketing techniques and technology is recounted in Stone, *Direct Marketing: Then and Now, Direct Marketing,* May 1988, p. 38.

[5] *Time,* November 26, 1990, at p. 66.

[6] These figures are from the Direct Marketing Association, as reported in their special advertising section in the March 14, 1991, edition of USA Today, at pp. 10A-11A.

[7] See *Time,* November 26, 1990, at p. 63; *Direct Marketing,* July 1990, at p. 30.

[8] As the Supreme Court noted in *Mobil Oil Corp. v. Commissioner of Taxes of Vermont,* 445 U.S. 425, 443, 100 S.Ct. 1223, 1234, 63 L.Ed.2d 510, 524 (1980), "[t]he effect of the Commerce Clause on state taxation of interstate commerce . . . appears to be undergoing a revival of sorts" and "this Court has addressed the issue and has attempted to clarify the apparently conflicting precedents it has spawned."

[9] Empirical studies have demonstrated the effect of the presence or absence of sales or use taxes upon consumer purchasing behavior. See, e.g., Mowen, Wiener & Young, *Consumer Store Choice and Sales Taxes: Retailing, Public Policy, and Theoretical Implications,* 66 Journal of Retailing 222 (1990).

[10] This argument is also undermined in this case by Quill's extensive computer expertise. Quill sells computers and related hardware, and has developed its own computer software to allow customers to contact Quill directly on their own computers to place orders, check price and availability, and communicate via an electronic bulletin board.

[11] Quill did not, in fact, place its arguments within the context of the *Complete Auto* test, which clearly governs review of a Commerce Clause challenge to a use tax. See *Holmes, supra.*

[12] No assertion has been made that the use tax is not fairly apportioned or that it discriminates against interstate

commerce. Thus, the second and third prongs of the *Complete Auto* test need not be addressed.

[13] The State argues that Quill owns other property in North Dakota, providing a further showing of nexus and benefits. The State asserts that Quill makes sales on approval in North Dakota and retains title to the goods until the merchandise is accepted or rejected by the buyer. Thus, the State argues, Quill owns property within the State which receives fire and police protection, as well as other benefits.

Quill's catalog makes the following offer to customers:

> "Use any product from Quill in your office FREE for 30 days. During that time, try it, inspect it, use it . . . just to be sure you're satisfied with the product. You have no reason to pay us and can return it during that period for any reason . . . no questions asked . . . and we'll give you a full credit against your invoice."

In addition, customers may, at any time within 90 days of purchase, return any item for a full refund if not completely satisfied.

Section 41-02-43(1), N.D.C.C., [U.C.C. § 2-326] provides:

> *"Sale on approval and sale or return — Consignment sales and rights of creditors.*
>
> "1. Unless otherwise agreed, if delivered goods may be returned by the buyer even though they conform to the contract, the transaction is:
>
> "a. A 'sale on approval' if the goods are delivered primarily for use.
>
> "b. A 'sale or return' if the goods are delivered primarily for resale."

If a transaction constitutes a sale on approval under Section 41-02-43(1), title to the goods does not pass until the buyer accepts them. Section 41-02-44(1)(a), N.D.C.C.

Quill asserts, however, that its sales are not "sales on approval" because it does not offer an "unconditional guarantee of refund" and because in some cases the buyer must pay the return shipping costs.

The district court summarily rejected the State's argument and ruled that, as a matter of law, title to the merchandise passed to the purchaser immediately at the time of shipping. Although the court's ruling was wholly conclusory and failed to fully take into account the underlying factual issues necessary to a determination of the legal issues, we find it unnecessary to resolve this issue at this time. Because we have held that sufficient nexus exists to support imposition of the duty to collect and remit the use tax, we need not determine if Quill has additional nexus with the State through retention of title to goods sold on approval.

[14] It is estimated that 44% of all such direct mail solicitations are disposed of unopened and unread. *Time*, November 26, 1990, at p. 64.

[15] Recent estimates indicate that such "junk" mail "is now a nearly 4 million-ton colossus that accounts for 39% of all U.S. postal volume. This year about 41 lbs. of junk mail have been generated for each adult American." *Time*, November 26, 1990, at pp. 63-64.